

*United States Court of Appeals
for the
District of Columbia Circuit*



**TRANSCRIPT OF
RECORD**

652

IN THE
UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT

No. 22,994

J. HENRY POLKINHORN,
Executor of the Estate of Grace B. Affleck, Deceased
and

JOHN H. POLKINHORN,
Trustee of the Testamentary Trust under the Will of
Philip G. Affleck, Deceased,

Appellants,

v.

THE UNITED STATES OF AMERICA,

Appellee.

APPEAL FROM THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLUMBIA

United States Court of Appeals
for the District of Columbia Circuit

FEB 2 1970

APPENDIX

John H. Polkinhorn
John H. Polkinhorn
Clerk

12994

(i)

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CIVIL DOCKET

United States District Court for the District of Columbia

NUMBER

2555-66

ACTION FOR

REFUND OF FEDERAL INCOME TAXES

PARTIES	ATTORNEYS
1. VENNY POLKINHORN, Executor of the Estate of GRACE B. AFFLECK, Deceased and JOHN H. POLKINHORN, Trustee of the Testamentary Trust under the Will of PHILIP G. AFFLECK, Deceased	W. Barrett McConnell 430 Washington Blvd.
THE UNITED STATES OF AMERICA	Mitchell Rogovin Myron C. Baum Dept. of Justice
	Jury demand <input checked="" type="checkbox"/>

CIVIL DOCKET

United States District Court for the District of Columbia

DATE	PROCEDURAL
1966	
Oct. 21	Deposit for cost by Plaintiff, appearance and Jury demand. filed
Oct. 21	Summons, copies (2) and copies (2) of Complaint issued DA ser 10/31/66; AG ser 11/5/66.
Dec. 29	Answer of deft to complaint; c/m 12/27/66; Appearance of Mitchell Ropovin, Myron C. Baum. filed
Dec. 29	Calendar (1/1/67) (N)
1967	
Apr. 13	Called. Assistant Pretrial Examiner
Sep. 13	First Notice of Trial. (N)
Oct. 10	Certificate of Readiness by Plaintiff; c/m 10/9/67. filed
Oct. 20	Objection of defendant to plaintiff's Certificate of Readiness; c/m 10/20/67. filed
Nov. 9	Recommendation sustaining defendant's objection to certificate of readiness; case to be placed on calendar as of February 1, 1968. AC/N. Assistant Pretrial Examiner
1968	
Sept. 17	Plaintiff Stipulation. Plaintiff waives request for Jury Trial. (Consent) Stipulation with exhibits. Pretrial Examiner
Oct. 21	Deposition of John Henry Polkikhorn for deft. Exhibit 1. Filed
Dec. 3	Hearing term; rescheduled to Dec. 4, 1968. (Rep. Simon Banks, Jr.) Holtzoff, J.
Dec. 4	Hearing rescheduled; Plaintiff for defendant. (Judgment to be prepared) (Rep. Simon Banks, Jr.) Holtzoff, J.
Dec. 4	Trial brief of defendant; c/a 10/21/68. filed
Dec. 17	Corrected copy of oral opinion delivered from the bench on Dec. 1, 1968. (N) Holtzoff, J.
Dec. 20	Judgment for defendant and dismissing the complaint on the merits. (N) Holtzoff, J.
Dec. 27	Motion of Plaintiff for new trial, for amendment of finding of fact and conclusions of law; PWA; c/m 12/27/68. i.c. filed
1969	
Jan. 10	Opposition of deft. to motion for new trial, for amendment of finding of fact & conclusion of law. c/a 1/10/69. filed
Jan. 13	Motion of Plaintiff, for new trial, for amendment of findings of fact and conclusions of law, DEFNIT. (Fiat) (N). Holtzoff, J.
1970	
Mar. 6	Notice of Appeal by Pltf from Order of 12/20/68. \$5.00 deposit by W. McDonnell; copies to Attorney General and U. S. Attorney. filed
Mar. 6	Cost Bond on Appeal by Pltf in sum of \$250.00 with Travelers Indemnity Company; Approved. file
Apr. 29	Preliminary Record on Appeal delivered to USCA; Deposit by W. Barrett McDonnell 80¢
Apr. 29	Receipt from USCA for Preliminary Record fil

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLUMBIA

J. HENRY POLKINHORN, Executor of the
Estate of Grace B. Affleck, Deceased.

and

FILED

OCT 28 1966

JOHN H. POLKINHORN, Trustee of the
Testamentary Trust under the Will
of Philip G. Affleck, Deceased,
2737 Devonshire Place, N. W.
Washington, D. C.

ROBERT M. STEARNS, CLERK

JURY
ACTION

Plaintiffs

vs.

Civil Action No.

2888-66

THE UNITED STATES OF AMERICA

Defendant

COMPLAINT FOR REFUND OF FEDERAL INCOME TAXES
ILLEGALLY AND ERRONEOUSLY COLLECTED

1. Jurisdiction is conferred by Section 1346 (a) of Title 28
of the United States Code (1958 ed.)

2. Plaintiff J. Henry Polkinhorn, is the duly appointed,
qualified and acting Executor of the Estate of Grace B. Affleck,
deceased, who died a resident of the District of Columbia on
June 20, 1964, and he brings this action as the personal
representative of the Decedent's Estate.

3. Plaintiff, John H. Polkinhorn (who is the same individual
as Plaintiff J. Henry Polkinhorn), is the duly appointed,
qualified and acting Trustee of the Testamentary Trust established
by the Will of Philip G. Affleck, deceased, who died a resident

of the District of Columbia on January 7, 1947, and he brings this action as such Trustee.

4. During the calendar year 1960, the said Grace B. Affleck, deceased, was life tenant of the Estate of Philip G. Affleck, deceased, with full power to lease real property constituting the corpus of the said life estate, and during the calendar year 1960 she did so lease a parcel of real estate in the life estate for a term of 99 years for and at a fixed minimum annual rental.

5. Plaintiff John H. Polkinkhorn, as Trustee, joined in said lease as Lessor, and the vested remaindermen of the Trust Estate approved said lease.

6. Among the terms and conditions of the said lease was a provision that the Lessee would assume the obligation of the Lessor's promissory notes for \$27,500.00, secured by a first deed of trust to the said parcel of real estate, and could, on any interest date, pay and discharge said indebtedness, and, in any event, was required to discharge such indebtedness prior to razing the improvement then standing on the leased premises, which improvement was declared to be the property of the Lessee.

7. On or about December 10, 1960, the Lessee did so pay and discharge the said indebtedness of \$27,500.00 and razed the improvement.

8. Thereafter, the defendant, through its agent, the Internal Revenue Service and its District Director at Baltimore, Maryland, required Grace B. Affleck, deceased, to include the

said amount of \$27,500.00 in gross income received by her in the calendar year 1960, and assessed against her and required her to pay, and she did pay, the sum of \$8,802.68 as additional individual income tax, by reason of inclusion of the said \$27,500.00 in her gross income for the year 1960 and by reason of other adjustments not now contested, together with interest thereon in the amount of \$1,293.73 from April 15, 1961, to the date of payment.

9. The inclusion of the aforementioned sum of \$27,500.00 in gross income to the decedent and assessment and collection of the aforementioned tax by the defendant, as aforesaid, was erroneous and illegal, and contrary to the provisions of Section 108 of Title 26 of the United States Code and the Regulations issued pursuant thereto, and the plaintiff was and is entitled, as the personal representative of the decedent, to claim, demand and to have a refund of such taxes and interest assessed and paid with interest thereon.

10. Plaintiff has demanded a refund of the aforesaid income taxes paid, on the ground that the same was erroneously and illegally demanded and collected from the decedent, and has complied with the provisions of Section 108 and all other applicable provisions of Title 26 of the United States Code and other provisions of law, and his demands for refund of the said payment were refused by the defendant on or about November 4, 1964.

11. Plaintiff, John H. Polkinhorn, Trustee of the Testamentary Trust established by the Will of the said Philip G. Affleck, deceased, joins in this action as Plaintiff on the ground that if the said sum of \$27,500.00 is held to be income, then it is income to the Trust under the Will of Philip G. Affleck, deceased, permanently set aside for charitable uses under Section 642(c) of Title 26 of the Internal Revenue Code, and, as such, is exempt from income tax as an increase in the equity of the remaindermen or as a return of principal of the Trust of which the life tenant was then constructive trustee, and of which the plaintiff John H. Polkinhorn is now acting trustee.

WHEREFORE, the Plaintiffs demand judgment against the defendant for so much of the sum of \$10,096.00, with interest thereon, as represents additional individual income tax imposed and paid as a result of inclusion of the sum of \$27,500.00 in the gross income of Grace B. Affleck, deceased, for the year 1960, together with interest thereon.

Estate of Grace B. Affleck, Deceased.

John H. Polkinhorn
John H. Polkinhorn, Executor

W. Barrett McDonnell
W. Barrett McDonnell
Attorney for Plaintiffs
Suite 430, Washington Building
Washington, D. C.

John H. Polkinhorn
John H. Polkinhorn, Trustee of Testamentary
Trust under Will of Philip G. Affleck,
Deceased, 2737 Devonshire Place, N. W.,
Washington, D. C.

Plaintiffs

DISTRICT OF COLUMBIA: ss

J. Henry Polkinhorn, being duly sworn, deposes and says that he resides at 2737 Devonshire Place, N. W., Washington, D. C.; that he is the plaintiff herein under the name of J. Henry Polkinhorn and the name of John H. Polkinhorn; and that he has read the foregoing complaint and knows the contents thereof and that the same are true of his own knowledge except as to the matters therein stated to be alleged on information and belief, and as to those matters he believes them to be true.

J. Henry Polkinhorn
J. Henry Polkinhorn

Subscribed and sworn to before me this 28th day of

October, 1966.

Sophie E. Birkhead
Notary Public, D. C.

MY COMMISSION EXPIRES JUNE 14, 1971.

DEMAND FOR JURY TRIAL

Plaintiffs herein demand a jury trial.

J. Henry Polkinhorn
J. Henry Polkinhorn

John H. Polkinhorn
John H. Polkinhorn

[Caption Omitted in Printing]

A N S W E R

The defendant, the United States of America, by and through its attorneys, for its answer to the complaint herein alleges as follows:

1. Denies the allegations contained in paragraph 1.
2. Denies knowledge or information sufficient to form a belief as to the truth of the allegations contained in paragraph 2.
3. Denies knowledge or information sufficient to form a belief as to the truth of the allegations contained in paragraph 3.
4. Denies knowledge or information sufficient to form a belief as to the truth of the allegations contained in paragraph 4.
5. Denies knowledge or information sufficient to form a belief as to the truth of the allegations contained in paragraph 5.
6. Denies knowledge or information sufficient to form a belief as to the truth of the allegations contained in paragraph 6.
7. Denies knowledge or information sufficient to form a belief as to the truth of the allegations contained in paragraph 7.
8. Admits the allegations contained in paragraph 8.
9. Denies the allegations contained in paragraph 9.
10. Admits that plaintiff has demanded a refund for the income taxes paid and that such demand for refund was refused by defendant on or about November 4, 1964. Defendant denies all other allegations contained in paragraph 10.
11. Denies the allegations contained in paragraph 11.

AFFIRMATIVE DEFENSES

12. By way of further and more complete defense to plaintiff's claim, defendant alleges as follows:

a) Jurisdiction of suits against the United States seeking a refund of income taxes alleged to have been erroneously and illegally assessed and collected is vested in the District Courts pursuant to 28 U.S.C. Sec. 1346(a).

b) Prerequisite to a proper suit over which the District Courts can take jurisdiction, however, is fulfillment of the provisions of Sections 6511, 6532, and 7422 of the Internal Revenue Code of 1954. These provisions require a plaintiff to:

- 1) pay the tax;
- 2) file a claim for refund;
- 3) institute suit.

c) Unless these requirements are met, no District Court can take jurisdiction of any suit for refund of taxes.

d) Plaintiff, John H. Polkinhorn, Trustee of the Testamentary Trust under the Will of Philip G. Affleck, Deceased, has failed to meet each and every one of the above-stated prerequisites.

e) Therefore, this Court does not have jurisdiction of this action as to said plaintiff, and it should accordingly dismiss this suit as to said plaintiff.

13. By way of further and more complete defense to plaintiffs' claim, defendant alleges as follows:

a) Rule 8(a) of the Federal Rules of Civil Procedure requires both a short and plain statement of the basis of the Court's jurisdiction and a short and plain statement of the pleader's claim for relief.

b) Plaintiff John H. Polkinhorn, Trustee of the Testamentary Trust under the Will of Philip G. Affleck, Deceased, has failed to present either of these statements.

c) Therefore, the complaint is inadequate as to said plaintiff and should accordingly be dismissed.

14. By way of further and more complete defense to plaintiffs' claim, defendant alleges as follows:

a) District Courts are barred from granting declaratory judgment relief in federal tax matters by the provisions of 28 U.S.C. Sec. 2201 and 26 U.S.C. Sec. 7421.

b) Therefore, this Court lacks jurisdiction of the complaint to the extent it requests such relief.

WHEREFORE, defendant prays that judgment be entered in its favor, dismissing plaintiffs' complaint, allowing defendant its costs and such other and further relief as this Court may deem just and proper.

Mitchell Rogovin

MICHELL ROGOVIN
Assistant Attorney General

Myron C. Baum

MYRON C. BAUM
Attorneys, Tax Division
Department of Justice

Attorneys for Defendant

Of Counsel:

David G. Bress
DAVID G. BRESS *per se*
United States Attorney

[Certificate of Service Omitted in Printing]

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLUMBIA

-----x
J. HENRY POLKINHORN, Executor of
the Estate of Grace B. Affleck,
Deceased,

and

JOHN H. POLKINHORN, Trustee of
the Testamentary Trust under the
will of Philip G. Affleck,
Deceased,

Civil Action No. 2888-66

Plaintiffs,

v.

THE UNITED STATES OF AMERICA,

Defendant.

-----x
Washington, D. C.
Monday, January 15, 1968

Deposition of

JOHN HENRY POLKINHORN,

called for examination by counsel for the defendant, pursuant to
agreement, in room 5122, Justice Department, Tax Division,
1101 Pennsylvania Avenue, N.W., Washington, D. C., beginning at
1:40 p.m., before Albert R. Sparks, a Notary Public in and for
the District of Columbia, when were present on behalf of the
respective parties:

For the Plaintiffs:

W. BARRETT McDONNELL, ESQ.
430 Washington Building
Washington, D. C. 20005

For the Defendant:

DANIEL L. PENNER, ESQ.
Tax Division, Department of Justice
Washington, D. C. 20530

PROCEEDINGS

Whereupon,

JOHN HENRY POLKINHORN

was called for examination by counsel for the defendant and, having been first duly sworn by the Notary Public, was examined and testified as follows:

MR. MC DONNELL: Let the record show that Mr. Polkinhorn appears voluntarily in response to a request from Government counsel in lieu of formal notice under the rules of the court.

MR. PENNER: Let the record show that counsel stipulates the waiver of the requirement of notice and signing of the deposition.

DIRECT EXAMINATION

By Mr. Penner:

Q Would you state your full name?

A Which way? I use the name J. Henry Polkinhorn and John H. Polkinhorn.

Q What is your address?

A 2737 Devonshire Place, Northwest, apartment 314, Washington, D. C.

Q Are you the plaintiff in this lawsuit?

A Yes.

Q Did you know Mrs. Grace B. Affleck?

A That was my mother.

Q And what connection do you have with the estate of Mrs. Affleck?

A Well, I guess I am executor in her estate.

Q And what connection did you have with the estate of Mr. Affleck?

A I am trustee in the estate now.

MR. PENNER: Off the record.

(Discussion off the record.)

By Mr. Penner:

Q Mr. Polkinhorn, are you aware that Mr. Affleck conveyed certain property, real property, which is the subject of this lawsuit, to Mrs. Affleck by his will, giving her a life estate?

A A life estate, but not property given to her.

Q I see. What was the date of the death of Mr. Affleck?

A January 7, 1947. Wait a minute. Yes, I am sure it is January 7, 1947. Yes.

Q All right. The property that we are concerned with is 1862 M Street, Northwest, is that correct?

A That is correct, sir. It was known as 1826, but it is not that number now.

Q What is the number now?

A I do not know, sir.

Q Then are you aware that on June 10, 1958, the taxpayer, Mrs. Affleck, executed three notes secured by a first deed of trust on that property?

A I have heard of it. I don't know about it.

I don't know the date, either, for that matter. You say 1958.

I wouldn't know that.

Q I see. On the 28th of September 1960, that property was leased by Mrs. Affleck and yourself as trustee to the Ring family, is that correct?

A As far as I know. I am not sure of the date, but it was to Gustave Ring.

MR. PENNER: Off the record.

(Discussion off the record.)

MR. PENNER: I hand this lease agreement to the reporter and ask that he mark it as Government Exhibit 1 for identification.

(A copy of a lease agreement was marked for identification as Government Exhibit 1.)

MR. PENNER: Off the record.

(Discussion off the record.)

By Mr. Penner:

Q I hand you, Mr. Polkinhorn, the lease agreement and ask if that is the agreement you have executed as trustee.

A Yes, sir.

Q Does that agreement call for discharge of a debt of the landlord's as partial payment of rent?

A I beg your pardon.

Q Does that agreement call for, in partial payment of the rental due, the discharge by the tenant of the landlord's indebtedness?

A Do you mean the person to whom we rented this property, were they going to take care of the mortgage on this property? Is that what you mean?

Q No, it is my understanding, and you said you had heard that Mrs. Affleck executed three notes in 1958 in the total amount of---

A I don't know whether there were three notes or not. As I recall, there was about a \$17,000 mortgage on it, and I think mother borrowed about \$10,000 more, and it was \$27,000-plus.

Q \$27,500?

A That was for the improvement of other property that belonged to Mr. Affleck's estate.

Q Did this agreement call for the payment of that indebtedness as partial payment of the rent on the property?

MR. MC DONNELL: Can we go off the record?

(Discussion off the record.)

MR. PENNER: Back on the record.

By Mr. Penner:

Q I am referring to the fifth line from the bottom, beginning there "for a term of 99 years" and ending "the 9th day of October at and for a total rental of not less than \$1,017,500, payable by discharge by the tenant, as hereinbelow provided," and on over to page 2.

I ask you again: Did this lease call for partial payment of the total rental due, the discharge by the tenant of

the landlord's indebtedness?

A The Ring organization was to pay the mortgage of 27,500 off when they rented the building. They offered 12,000 a year at first, clear, and then they offered 10,000 a year and they would take care of the 27,500.

Q All right.

A Does that answer your question?

Q That answers it, yes.

You don't know when Mrs. Affleck borrowed the \$27,500?

A I do not, sir.

MR. PENNER: Off the record.

(Discussion off the record.)

MR. PENNER: Back on the record.

By Mr. Penner:

Q Mr. Polkinhorn, prior to the execution of this lease, in what manner was the property used during the period from the date of Mr. Affleck's death until the execution of this lease?

A This so-called property we are speaking of now, 1826?

Q Right.

A As I recall, it was a four-story brick apartment house, and it was in such poor condition that the attorney previous to Mr. McDonnell---

Q What was that attorney's name?

A Mr. John Myers. He is deceased -- John Myers. He was thinking in terms of renovating this whole building and renting

it out, but the cost was prohibitive. And then he talked about tearing it down and using it for parking space.

The inspectors were after us all the time about it. It was one of those kinds of buildings that certain persons live in, and you would fix something one day and the next day it would be broken out. It was in foul shape.

Q. Was it at that time rented?

A. At the time it was sold?

Q. At the time of this lease agreement.

A. It was rented in part. I don't know whether it was in full or not.

Q. It was partially occupied?

A. Yes, partially leased.

MR. PENNER: Off the record.

(Discussion off the record.)

MR. PENNER: Back on the record.

By Mr. Penner:

Q. It is my understanding, Mr. Polkinhorn, that when Mrs. Affleck executed the notes in question, some \$27,000 worth of notes, that the proceeds of those notes were applied, approximately \$16,800 to existing indebtedness on the property, and the remaining sum, approximately \$10,500, was paid to her cash-in-hand.

Do you remember whether that is substantially correct?

A. I don't know a thing about this.

My understanding was that this property had encumbrances on it for about 17,000 and that Mrs. Affleck put additional -- approximately 10,000-plus -- on it. I know nothing about her receiving any cash in hand. I know nothing about that.

Q What would be the proceeds of the \$10,000? How would that be applied?

A That was to take care of other property. We were in bad shape financially.

Q So the 10,000 was used for improvements on other property?

A And it could have been used also to pay off on a lien on another piece of property. I can't tell you, sir. It was just my understanding. I don't know.

MR. MC DONNELL: Off the record again?

MR. PENNER: Yes.

(Discussion off the record.)

MR. PENNER: Back on the record.

By Mr. Penner:

Q Mr. Polkinhorn, when were you appointed as trustee?

A To the best of my recollection, March 17, 1960.

THE WITNESS: Off the record for a moment?

MR. PENNER: Yes.

(Discussion off the record.)

By Mr. Penner:

Q Mr. Polkinhorn, what was Mrs. Affleck's occupation during

the year 1960?

A Well, none.

Q Did she have any other rental property? Did she own any other rental property or have any other interest in other rental property?

A Her deceased husband's property, under the Affleck will, That is all.

Q There were other properties other than this particular property, the income from which was distributed to her?

A Which she received, yes.

Q Then you would say that the trust was, in 1960, in the business of managing the property of the deceased, Mr. Affleck?

A Myself, or my mother?

Q The trust.

A The trust?

Q Of which you were trustee.

A Excuse me?

Q Was the trust engaged in business?

A I don't understand that question.

Q What assets were in the trust in 1960?

A Interest from the property, rentals from the property.

Q But was the property itself in the trust? What were the assets of the trust?

A I can't answer that, sir.

Q Perhaps you can ask your counsel.

MR. MC DONNELL: Do you want me on the record to advise him?

MR. PENNER: Yes.

MR. MC DONNELL: What date are we speaking of?

MR. PENNER: 1960.

MR. MC DONNELL: The date of the execution of this lease?

MR. PENNER: Yes.

MR. MC DONNELL: I am a little taken aback. If I may, so that I don't appear on the record to be advising my client of the answers, may I do this by questioning?

MR. PENNER: If you prefer.

MR. MC DONNELL: In 1960, as of the date of your appointment as trustee under the will of Philip Affleck, deceased, did you as trustee have title to any properties?

THE WITNESS: I did not.

MR. MC DONNELL: Where was the title of the properties in 1966?

THE WITNESS: I presume under Mrs. Affleck, if I understand your question.

MR. MC DONNELL: In what capacity?

THE WITNESS: She was life tenant.

MR. MC DONNELL: Do you recall the properties that were in the name of the life tenant as of the date of the execution of this lease in September 1960?

THE WITNESS: I would have to go back on your records of what was sold and what wasn't sold.

MR. MC DONNELL: May I help you, then, if there would be no objection to a few leading questions?

Did the estate of Philip G. Affleck, deceased, own any properties on Pennsylvania Avenue, Northwest?

THE WITNESS: Yes, sir.

MR. MC DONNELL: What was the address of those properties?

THE WITNESS: I believe it was 2421 and 2423 Pennsylvania Avenue, Northwest.

MR. MC DONNELL: Did the same estate have any properties on O Street?

THE WITNESS: Yes, 1206 O, Northwest, and 1209 O Street, Northwest.

MR. MC DONNELL: Did the estate at that time have any properties on P Street, Northwest?

THE WITNESS: Yes, sir.

MR. MC DONNELL: Do you recall the address of those properties?

THE WITNESS: No, sir, I do not. It was on the north side of P Street. There were about five buildings, nearer 14th Street than 15th Street. One of them had a big automobile place inside, a repair shop, an open-air repair shop. And they were two-story buildings.

MR. MC DONNELL: Did the estate own any properties on 11th Street, Northwest?

THE WITNESS: Yes, sir.

MR. MC DONNELL: Do you recall the address of those properties?

THE WITNESS: About 1405 to 1411 or 1413, on the east side.

MR. MC DONNELL: If I told you the addresses were 1411 to 1419, would that refresh your recollection?

THE WITNESS: It could be.

MR. MC DONNELL: Were there any other properties in the estate on 11th Street?

THE WITNESS: Yes, there was one property, in the 1700 block, about 1725 - 11th Street. That was a single house. I believe it was a two-story house.

MR. MC DONNELL: Did the estate have any properties on 14th Street, Northwest?

THE WITNESS: 14th and V Streets, Northwest.

MR. MC DONNELL: Did the estate own any other properties on 14th Street?

THE WITNESS: Yes, yes, yes. In the 1200 block of 14th Street. I believe there were either two or three buildings on the west side of the street, right across from the big Lutheran Church there. It would have been two buildings or three buildings. One of them was rented, I believe.

MR. MC DONNELL: Was rented by whom?

THE WITNESS: By Mr. Affleck.

MR. MC DONNELL: Did the estate own any properties on South Capitol Street, Southeast?

THE WITNESS: We had a piece of property in the 1100 block of New Hampshire Avenue that was sold. I do not recall whether we had the South Capitol Street property at this time or not.

MR. MC DONNELL: Why do you associate it with the New Hampshire Avenue property?

THE WITNESS: It seems to me when we sold New Hampshire Avenue, we had to invest the money, and that is when we bought some property down there. I am not sure. We did have our house on Maple Street in Takoma Park. I believe it was Maple Street out there, a two-story wooden house.

MR. MC DONNELL: I guess that is all.

MR. PENNER: All right.

By Mr. Penner:

Q Mr. Polkinhorn, these assets were not in the trust?

A I don't know what you mean by "assets were not in the trust." I don't know what you mean by that. Sorry.

MR. PENNER: Off the record.

(Discussion off the record.)

By Mr. Penner:

Q Mr. Polkinhorn, the notes that we have referred to in

the amount of \$27,500, were those notes paid off by the tenant of the property at 1826 M Street?

A By Mr. Ring, or Mr. Ring's associates.

Q When were those notes paid off?

A When he took possession of the property.

Q Would that be in 1960?

A It could be. It would be in the late part of 1960.

Q Did Mrs. Affleck ever make any payments on the notes, to your knowledge, payments of either interest or principal?

A On what notes, sir?

Q On the notes that were paid off by Ring---

A Not that I know of. I would say no.

You mean the 27,500?

Q Yes.

A That was paid by Ring.

Q She never made any payments on the notes?

A Not that I know of, sir.

MR. MC DONNELL: I am sorry, but I don't think the witness understood the full question. You said payments as to principal and interest.

THE WITNESS: Oh. She paid the government some money.

Is that what you mean?

By Mr. Penner:

Q No, did she ever pay any interest on the principal amount of the notes?

A I do not know, sir.

MR. PENNER: Off the record.

(Discussion off the record.)

By Mr. Penner:

Q Mr. Polkinhorn, during the year 1960 and prior to that time, who took care of the management of the properties of which Mrs. Affleck was life tenant?

A After the death of Mr. Affleck, Mr. Jan Beller. He had worked for Mr. Affleck for a number of years in the drug business and also in the real estate business. To the best of my recollection, he took care of it in the office that Mr. Affleck had at 2423 Pennsylvania Avenue.

Then Mrs. Affleck's attorney, Mr. Horton Lester, passed away. Before he passed away, he recommended that John J. Myers become Mrs. Affleck's attorney, and Mr. Myers handled things for my mother up until some irregularities occurred and he became ill,

Then Mr. Daniel O'Connor, an attorney, took over for a short time until he became head of the Internal Revenue investigating department.

Then Mr. McDonnell took over.

Q As of what date did Mr. McDonnell take over?

A I couldn't tell you that, sir -- before I became trustee and so forth.

Q Before you became trustee?

A Before, yes.

Q So before 1960, Mr. McDonnell was handling the management of the properties for your mother?

A No. Thomas D. Walsh Realty Company. I believe they are at 1900 K Street, Northwest.

Q How long did the Thomas D. Walsh Realty Company handle the management of the properties for your mother?

A They are handling them at the present time.

Q When did they begin handling those properties?

A Right after -- either after Mr. O'Connor or Mr. McDonnell took over. I don't know.

Q Prior to 1960?

A Yes, sir, to the best of my recollection.

Q Mr. Polkinhorn, was the \$27,500, which represented a debt discharged by the tenant of the property at 1826 M Street, reported as income on the 1960 return of Mrs. Affleck?

A I do not know. You will have to ask Mr. McDonnell that.

Q Would you ask Mr. McDonnell and refresh your recollection?

MR. MC DONNELL: No. It was not.

THE WITNESS: Mr. McDonnell says it was not.

By Mr. Penner:

Q Is that your recollection?

A I don't recollect, sir. Sorry.

Q Then if it were not included on the income-tax return of

Mrs. Affleck for 1960, then you wouldn't know why it was not included?

A No, except that Mrs. Affleck didn't receive the \$27,500. It was paper, and it went to the estate. She had nothing to do with that.

Q But it was a cancellation of indebtedness?

A Against the Affleck estate.

Q Then at the time that return was filed, was there a consent to reduction as prescribed in section 1017 of the Revenue Code and required by section 108 of the Revenue Code? Was that filed with the original return?

A I do not know, sir.

Q Do you know if there was ever a consent filed?

A I do not know, sir.

Mr. McDonnell advised us, my mother and myself, on all these things, and he gives good advice.

Q In 1960, was the property at M Street advertised for rent?

A You mean the apartment that was there?

Q Yes.

A I do not recall that, sir.

Mr. Ring, who had the building on the southeast corner of 19th and M Streets, as I recall, wanted to build -- he had a garage there, and he wanted to build over the top of it a number of stories so he could rent it for office space. He did

not have an entranceway to his elevators and so forth.

I don't know whether he came to us or what the story was. I imagine he knew that we wanted to get rid of the building or something.

He offered so much for the building, and we rented to him on a 99-year lease with the proviso that any building he put on the property at 1826 would be attached to his own property, to cover us in case anything happened to his business and so forth.

I don't recall whether that property was put up for rent before Ring came along or not.

I do recall that several people had tried to get that property before Ring.

MR. PENNER: That is all the questions I have.

MR. MC DONNELL: May I cross examine?

MR. PENNER: Certainly.

CROSS-EXAMINATION

By Mr. McDonnell:

Q Mr. Polkinhorn, just for purposes of clarification, what was your understanding of the method of operation of the estate of Philip G. Affleck during your mother's lifetime and prior to the time when Mr. O'Connor and I began to advise your mother in legal matters?

A What was the what?

Q What was the method of operation of the estate?

A Well, they had an office at 2423 Pennsylvania Avenue that, after Mr. Beller was deceased Mrs. Alder took over collecting rents up there.

Q Who handled the deposit of rents and the disbursement of funds?

A John J. Myers.

Q You have stated, I believe, that sometime shortly before 1960 there was a change in the method of operation.

What is your recollection of that change of the method of operation?

A Before what date?

Q Shortly before 1960.

A Well, I believe that after the Myers episode, I believe that we got a real estate company -- my mother retained a real estate company to take care of the property.

Q Do you recall whether that was done on recommendation of counsel?

A Yes, it was.

Q What counsel?

A I believe it was you, or it could have been Daniel O'Connor. But I believe it was you, Mr. McDonnell.

Q Then do I understand from your previous answers that after that date the collection of rents and the management of the properties were in the hands of Thomas D. Walsh, Incorporated, and legal matters pertaining to the estate were in the hands of

Mr. O'Connor?

A That is correct, sir.

Q According to your recollection, what was the reason why you were appointed by the United States District Court as trustee under the will of Philip G. Affleck?

A Because Mrs. Affleck asked me to be.

Q But there was a trustee. Why were you asked to be?

A Mr. Colton resigned.

Q Do you recall by whom your mother's income tax returns were prepared?

A How far back?

Q 1960 and thereafter.

A Myers, sir.

Q Did you examine Mrs. Affleck's income tax returns before they were signed by her?

A I believe I did, but I am not too sure. I believe she signed them after conferring with you. On her personal income tax, now, I am speaking.

Q In matters pertaining to the estate, were you consulted by me?

A Yes.

Q Were you consulted by me with regard to the lease on the property then known as 1826 M Street, Northwest?

A Yes.

Q Did I advise you as to the terms, the various offers to

purchase or lease the property at 1826 M Street?

A That is correct, sir.

Q Do you recall what I advised you concerning the offer of Gustave Ring?

A Yes, sir.

Q What is your recollection?

A That Mr. Ring was offering to take the property on a 99-year lease, \$12,000 a year, unencumbered, and at \$10,000 if he was to pay off the 27,500 which was against the property.

And you told me that that would not be taxable, in your opinion.

Q Do you recall in any further detail what my advice regarding the taxable nature of the transactions would be?

A Yes. This property -- the money did not go to Mrs. Affleck. It went to the estate, and she benefited not at all from the \$27,500. And it would go after her death, the property -- the interest would be in life for myself, Marion Affleck, Mr. Affleck's daughter, and myself, and remaindermen, who are charitable organizations, would take care of the taxes.

Q Did I advise you whether there would be a capital-gains tax in connection with this transaction in the event of a sale of the property?

A I believe you stated that it would be a capital-gains tax if the property were sold, yes.

Q Did I advise you of the tax consequences of the

assumption by Gustave Ring of the mortgage indebtedness on this property on M Street? Did I advise you?

A Yes.

Q Do you recall what my advice was?

MR. PENNER: I object to that. I don't think that is competent testimony.

MR. MC DONNELL: On what ground?

MR. PENNER: I think it calls for a legal conclusion.

MR. MC DONNELL: I am asking him whether he recalls what I advised him regarding the tax consequences. I am not asking him to draw a legal conclusion. I am asking him whether he recalls what I advised him as to the tax consequences.

MR. PENNER: All right.

THE WITNESS: You advised that we take the \$10,000, 99-year lease and that Mr. Ring would pay off the 27,500.

Q Did I advise you that there would be any tax liability to your mother or to the estate as a result of that?

A You stated that there would not be any tax liability.

Q What was the date of your mother's death?

A June 20, 1964.

Q What is your understanding of the legal consequences of her death with regard to the estate of Philip G. Affleck?

A Repeat that, please.

Q What is your understanding of the legal consequences of her death with regard to the estate of Philip G. Affleck?

Let me rephrase that. I am asking you for a legal conclusion.

When your mother died on June 20, 1964, did you then assume title to the properties as trustee of the estate of Philip G. Affleck?

A I did.

Q Did you thereafter become executor of your mother's estate?

A I did, sir.

Q Did I advise you after the execution of a lease on the property at M Street that the Internal Revenue Service had raised any question concerning the lease of this property?

A Not at the time, sir.

Q Did I thereafter?

A Yes, you did.

Q Did I advise you of the determination reached by the Internal Revenue Service?

A Well, as I recall, you told me that the Internal Revenue Service said that that 27,500 was taxable, which had been paid.

Q To whom?

A Against Mrs. Affleck, as personal property, which it was not.

I mean Mrs. Affleck did not receive the 27,500 herself.

Q When I advised you of the determination reached by

Internal Revenue, did I advise that your mother pay the tax?

A You did, sir.

Q Did I advise where the funds should come from to pay the taxes?

A From the Affleck estate, sir.

Q Do you recall why I advised that the funds be taken from the Affleck estate?

A Because Mrs. Affleck didn't benefit from the 27,500.

MR. MC DONNELL: I believe that is all I have.

REDIRECT EXAMINATION

By Mr. Penner:

Q Do you know, Mr. Polkinhorn, whether Mrs. Affleck, your mother, signed notes in the amount of approximately \$27,500?

A I do not. I never heard of that before.

Q Then what was the indebtedness to be discharged by the lease agreement dated 28 September 1960?

A That was the 27,500 that had been already borrowed, to my understanding -- about 17,000 by Mr. Affleck, and about 10,000-plus by my mother.

Q You will recall in our conversations thus far today that we had established, I thought, that your mother did in fact sign notes in the amount of \$27,500.

A Not to my knowledge, sir.

Q Would you look at page 3 of the lease and read paragraph 6 of that lease to yourself?

A Yes, sir.

Q Now I call your attention specifically to the second line of the fourth page of that agreement, wherein it states "certain promissory notes made by Grace B. Affleck," and ask you again: Did your mother, Grace Affleck, sign certain promissory notes in the amount of approximately \$27,500?

A I do not know, sir.

Q Does the lease recite that certain notes were made by her and that those notes were to be discharged as part of the rent payable under the lease?

A I can't answer that question.

Q You can read it again, then, if you would like to.

A It says here the three promissory notes were made by Grace Affleck, dated June so-and-so. I don't know whether she signed them or not.

Q She signed this lease, did she not?

A Yes, and I signed it, but I don't know what happened in 1958.

Q Would you disagree with the proposition that she did sign three notes in the amount of \$27,500?

A I can't tell you that, sir.

MR. PENNER: Off the record.

(Discussion off the record.)

MR. PENNER: Back on the record.

By Mr. Penner:

Q Mr. Polkinkhorn, I will ask you again---

A I am sorry.

Q ---did your mother sign three notes in the amount of approximately \$27,500, which were to be discharged as part of the rent payable under the lease?

A It says so. I presume she did.

Q All right. Now I am going to ask you another question.

You said, as I recall, in your answers to Mr. McDonnell's questions, that Mrs. Affleck received no benefit from this. Is that correct?

A As far as I know, that is correct, sir.

Q I will ask you a hypothetical question.

If you borrow \$500 from me and Mr. McDonnell pays me the \$500 in cancellation of your debt to me, have you received the benefit?

A Yes, I have.

Q But you didn't get the cash in hand; did you?

A No.

Q But you did receive a benefit by virtue of Mr. McDonnell paying off your note---

A But Mrs. Affleck did not receive anything from this.

The estate did.

Q You said in answer to my last question that Mrs. Affleck signed notes---

A That is right.

Q Now you are saying that she was not obligated on those notes. Is that correct?

A No, no. I am saying that Mrs. Affleck did what she was requested to do by the attorney. This money did not go to Mrs. Affleck.

Q This doesn't make any difference. What I am saying is, she owed an obligation, which was paid?

A She didn't owe an obligation. The estate did.

Q She signed the notes.

A Oh, yes.

Q In her personal capacity or as executor of the estate, or how did she sign them?

A As tenant for life.

Q But that would be in her personal capacity as life tenant?

A Yes.

Q All right, then she owed an obligation, which was paid by someone else, is that correct?

A I can't go along with that. I don't know that. As far as I know, she didn't owe the obligation. The estate owed it. I am sorry.

MR. PENNER: That is all I have.

RECROSS-EXAMINATION

By Mr. McDonnell:

Q If we assume from the recital in the lease that your mother signed notes in this amount, what was the security for payment of the principal amount of those notes?

A The property.

Q And in whose name was that property?

A Affleck's estate.

Q Could your mother have sold that property in her lifetime and taken the proceeds herself?

A She could not.

Q To the best of your knowledge, did your mother in her lifetime ever sell any of the property or devote any of the proceeds of loans on the property to her personal use?

A Absolutely not.

Q You have stated on direct examination that the estate of Philip G. Affleck comprised a considerable number of properties, which you have identified in some detail.

Do you recall whether there were loans on any of these other properties?

A As far as I know, all of the properties had loans on them.

Q Would the notes given for payment of those loans have been signed by your mother?

A Yes.

Q In what capacity?

A They would probably have been done by Mr. Affleck, unless Mrs. Affleck raised them before I came into the picture.

Q In the event she had refinanced the indebtedness on the property of Mr. Affleck's---

MR. PENNER: I will object to that.

There is no evidence that she did that.

MR. MC DONNELL: Then I will make it a hypothetical question.

Q If there were loans on any of the other properties, on notes signed by your mother during her lifetime and after Mr. Affleck's death, were those notes included as debts of your mother's estate after her death?

A Not that I know of.

Q Will you refer to page 3 of the lease before you and tell me what the rate of interest recited is on those notes?

A On page 3?

Q Identifying the notes that we have been discussing.

MR. PENNER: I think that is on page 4.

THE WITNESS: Now, what did you ask me?

BY MR. MC DONNELL:

Q Tell me what is the rate of interest on those notes there identified.

A 5-1/2 percent.

MR. MC DONNELL: Will counsel for the Government

stipulate that the annual interest on \$27,500 at 5-1/2 is \$1,512.50?

MR. PENNER: \$1,512.50. I will stipulate that the interest on \$27,500 at the rate of 5-1/2 percent, the annual interest, is \$1,512.50.

By Mr. McDonnell:

Q Mr. Polkinhorn, if I advised you that the annual interest at 5-1/2 percent on \$27,500 is \$1,512.50, will you please tell me whether, to your knowledge, this amount of interest was paid during your mother's lifetime on this indebtedness?

A I don't know, sir.

Q How is interest paid at the present time on the indebtedness on the properties in the Philip G. Affleck estate?

A It is held out at the end of each month and put in a banking account and then paid off, as far as I know.

Q Held out of what?

A Held out of the rents.

Q Is it your understanding that that was the same method of operation prior to your mother's death?

A It was, sir.

Q Would you say that the \$1,512.50 annual interest on the indebtedness was paid out of gross rent?

A I can't answer that.

Q I will state another question.

If the annual interest was \$1,512.50 and if Mr. Ring

would have leased this property at \$12,000 annually, if the property were clear of debt, and at \$10,000 annually if it were not cleared of debt, would you say that your mother benefited from the payment of this indebtedness by Mr. Ring?

MR. PENNER: I will object to that, on the grounds that it calls for a conclusion.

By Mr. McDonnell:

Q If your mother could have realized \$2,000 more per year in rents on this property and the annual interest was less than \$2,000 per year, would your mother have benefited through the discharge of this indebtedness?

A I don't think so.

Q I will ask only two further questions.

Was it your understanding that during your mother's lifetime she relied upon advice of counsel in all that she did with regard to the properties in the Philip G. Affleck estate?

A Definitely.

Q Would you identify counsel, while she was alive?

A Barrett W. McDonnell.

Q Did she rely on my advice with regard to the execution of this lease?

A Altogether.

Q You were requested to sign the lease. On whose advice did you rely?

A Attorney McDonnell.

MR. MC DONNELL: That is all I have.

MR. PENNER: Thank you, Mr. Polkinhorn.

(Whereupon, at 3:00 p.m. the taking of the deposition
was concluded.)

— — —

I have read the foregoing pages 1
through 33, inclusive, which contain a
correct transcript of the answers made
by me to the questions herein recorded.

JOHN HENRY POLKINHORN

CITY OF WASHINGTON)
) ss.:
DISTRICT OF COLUMBIA)

I, Albert R. Sparks, the officer before whom the foregoing deposition was taken, do hereby certify that the witness whose testimony appears in the foregoing deposition (pages 1-33, inclusive) was duly sworn by me; that the testimony of said witness was taken by me in shorthand to the best of my ability and thereafter reduced to typewriting under my direction; that said deposition is a true record of the testimony given by said witness; that I am neither counsel for, related to, nor employed by any of the parties to the action in which this deposition was taken; and further that I am not a relative or employee of any attorney or counsel employed by the parties thereto, nor financially or otherwise interested in the outcome of the action.

Albert R. Sparks
Notary Public in and for
the District of Columbia

My commission expires June 30, 1971.

Conformed Copy of
Lease

Trust under the Will of
Philip G. Affleck
to
Gustave Ring et al.

Lots 833 and
868
Square 140

Please Return to:

W. Barrett McDonnell
Suite 430, Washington
Building
Washington, D. C.
20005

THIS AGREEMENT

Made this 28th day of September, A. D., one-thousand nine
hundred and sixty (1960), between GRACE B. AFFLECK of Washington,
District of Columbia, first, tenant under the Will of Philip G.
Affleck, Deceased, and JOHN H. POLKIEPORT of Washington,
District of Columbia, trustee of the testamentary trusts
created by the said Will of Philip G. Affleck, Deceased,
parties of the first part (hereinafter sometimes referred to as
the Landlord), and GUSTAVE RING and MARION L. RING of Washington,
District of Columbia, and CARLYN RING COHEN of New York, New
York, parties of the second part (hereinafter sometimes referred
to as the Tenant):

WITNESS:

That for and in consideration of the rent herein reserved and
to be paid, and the covenants, agreements and conditions herein
contained, the Landlord does hereby lease and demise unto the

Tenant, and the Tenant does hereby take and hold as Tenant of the Landlord, the land now improved by the premises numbered 1826 K Street, Northwest, (the improvements thereon being the sole property of the Tenant), in the District of Columbia, the said land being designated for purposes of taxation as Lot 833 in Square 140 and Lot 833 in Square 140 of the Land Records of the District of Columbia, for a term of ninety-nine (99) years, commencing the 10th day of October, 1960, and ending the 9th day of October, 2059, at and for a total rental of not less than one million, seventeen Thousand, Five Hundred Dollars (\$1,017,500.00), payable by discharge by the Tenant, as herein below provided, of the Landlord's indebtedness accrued at the commencement of the term hereof by deeds of trust on the demised land, in a total amount of Twenty-seven Thousand, Five Hundred Dollars (\$27,500.00), and the balance payable in equal monthly installments of Eight Hundred Thirty-Three Dollars and Thirty-four cents (\$833.34) during the first twenty (20) years of the term hereof, and monthly installments of not less than Eight Hundred Sixty-Three Dollars and Thirty-four cents (\$833.34) during the remaining term hereof, the first installment to be paid on the 10th day of October, 1960, and the remaining installments payable in advance on the 10th day of each succeeding calendar month during the term hereof, beginning on the 10th day of November, 1960, at the office of

Thomas D. Walsh, Inc., or elsewhere in the District of Columbia, as the Landlord may from time to time designate.

I.

And the Tenant does hereby covenant and agree as follows:

(1) That the Tenant will, and does hereby, take and hold said land as tenant for the term of ninety-nine (99) years, as aforesaid.

(2) That the Tenant will pay the rent in the amounts and at the times and place herein specified, without deduction or demand.

(3) That the Tenant, in the name of the Landlord, will pay, or, at the Tenant's own risk and expense, will contest, all real estate taxes, special assessments, water and sewer rent or charges, and all other charges in the nature of tax or benefit assessments which may be levied, imposed, charged or assessed upon the demised land during the term hereof, and all taxes, license fees and other charges upon this lease or upon the leasehold interest herein created and upon any improvements erected upon the demised land during the term hereof, and upon demand by the Landlord, exhibit received bills or other evidence of payment of real estate taxes and special assessment taxes.

(4) That the Tenant will make and complete all improvements on the demised land free from all mechanic's liens and other claims on account of materials and labor and that the Tenant

will save the Landlord harmless from all damages which might arise by reason of work done on the demised land, and nothing herein contained shall be construed to confer upon the Tenant any right or authority to impose or permit to be imposed a mechanic's lien or other charge upon the fee of the demised land or the interest of the Landlord thereto, and that the Tenant, insofar as it shall be within its power, will do no act, nor omit to do any act, nor suffer to be done any act that would jeopardize the interest of the Landlord in the fee.

(5) That the Tenant will, during the entire term of this lease, at the Tenant's own cost, carry public liability insurance upon the ground and premises in the minimum amount of \$50,000/\$100,000, and, upon demand by the Landlord, deliver appropriate certificates evidencing the then-current contracts of such insurance.

(6) That the Tenant will, as part of and in reduction of the total rental herein reserved, assume the Landlord's obligations for repayment of principal and payment of interest after the commencement of the term of this lease on three certain promissory notes made by Grace B. Affleck, dated June 10, 1958, and payable June 10, 1961, with interest at the rate of 5-1/2% payable semi-annually on June 10 and December 10, and with the privilege of payment of installments in the amount of Five Hundred Dollars (\$500.00) or multiples thereof on any interest date, two of said notes, in the amounts of \$500

Thousand (\$9,000.00) and Five Thousand, Five Hundred Dollars (\$5,500.00), respectively, payable at the office of the American Security Corporation, Washington, D. C., and one of said notes, in the amount of Thirteen Thousand Dollars (\$13,000.00) payable at the office of the American Security & Trust Company, Washington, D. C., and all of said notes being secured by a first deed of trust, dated June 10, 1956, to National Savings & Trust Company, Trustee.

(7) That the Tenant will discharge the aforesaid indebtedness before the improvements standing upon the demised land at the commencement of the term hereof shall be razed.

(8) That if the Tenant razes the improvement now standing upon the demised land, any improvement thereafter erected upon the demised land during the first twenty (20) years of the term will be, physically and by use, joined to the improvement owned by the Tenant now standing upon the land immediately adjacent to the demised land, to wit, Lot 867 and Lot 869, in Square 140 of the land records of the District of Columbia.

(9) That, before completion of the improvement to replace the improvements standing on the demised land at the commencement of the term hereof, the Tenant will not, without the written consent of the Landlord, assign this lease or any portion of the term herein granted, or sublet the demised land or any part thereof, except to the purchaser, donee, devisee, grantee, or lessee as a part of the sale, gift,

bequest, grant or lease of the said adjacent land, to wit, Lot 867 and Lot 869 in Square 140, of the land records of the District of Columbia; provided, however, that the Tenant may at any time during the term hereof, without the consent of the Landlord, mortgage the leasehold estate and execute such assignments of the leasehold estate as may be necessary to secure independence, and in such case the Tenant shall advise the Landlord of the identity of the trustee or trustees under any assignment in trust of the leasehold estate or of the identity of the mortgagee or mortgagees of the leasehold estate; and provided, further, that in the event of any assignment or sublease the Tenant shall not be relieved of any obligations under this lease.

(10) That the Tenant will not use or suffer to be used the demised land for any disorderly or unlawful purpose.

II.

And the Landlord does hereby covenant and agree as follows:

(1) That the Landlord grants to the Tenant full and exclusive possession of the demised land and improvements thereon, without interference or interruption, during the full term of ninety-nine (99) years, except upon breach of the covenants, conditions and agreements contained herein.

(2) That the Landlord grants the Tenant the right to close the way now existing on the demised land (that portion designated for purposes of taxation as Lot 869 in Square 140

of the Land Records of the District of Columbia) and to make such use of such way, including the erection of improvements thereon, as the Tenant sees fit.

(3) That if the Landlord receives a bona fide offer for purchase of the demised land which the Landlord desires to accept, the same offer shall be submitted in writing to the Tenant, and the Tenant shall have fifteen (15) days from the date of receipt of such offer to meet the terms of such offer, and shall have an additional thirty (30) days for settlement of the purchase contract, and in that event, the Landlord will sell the demised land to the Tenant, and execute a deed of conveyance therefor.

(4) That the Landlord will not sell a portion only of the demised land except to the Tenant.

(5) That the Landlord will not convey, pledge, assign or give any interest in the demised land that would destroy or jeopardize the leasehold estate or diminish the value thereof.

(6) That the Landlord grants the Tenant the right to reuse, alter, repair, or reconstruct any improvements standing upon the demised land during the term of this lease, in whole or in part, and the right to construct improvements as the Tenant shall determine, subject to the provision of Paragraph I (6) above; provided, however, that any alterations, repairs, reconstruction or construction shall be in conformity with all applicable statutes and regulations relating to such improvements.

(7) That the Landlord grants to the Tenant, after completion of the improvement erected to replace the improvements standing upon the demised land at the commencement of the term hereof, the right to assign this lease or any portion of the term herein granted, or to sublet the demised land or any part thereof, or to mortgage the leasehold estate or any part thereof without the consent of the Landlord; provided, however, that in the event of any assignment or sublease the Tenant shall not be relieved of his obligations under this lease.

(8) In the event that the Tenant shall deem it necessary or desirable to take any action with respect to the demised land which requires the assent, signature or action of the Landlord, he shall give notice thereof to the Landlord, and in the event the Landlord does not, within a reasonable time after receipt of such notice, give such assent or supply such signature or take such action or notify the Tenant in writing of the reasons for refusal thereof, then and in that event the Landlord does hereby nominate, constitute and appoint the Tenant, and the Tenant's successors or assigns, as and for the Landlord's attorney-in-fact, for the Landlord and in the Landlord's behalf to assent, sign and take such action as the Landlord might personally; provided, however, that the Tenant is not hereby empowered to execute a deed of conveyance, mortgage or deed of trust of the demised land.

(2) That the Landlord grants to the Tenant the right and option to renew this lease for an additional term of ninety-nine (99) years from the expiration of the term herein granted, upon the same terms and conditions of this lease, such right and option to be exercised by the Tenant during the full calendar year immediately preceding the date of expiration of the term herein granted by notification in writing to the Landlord by registered mail addressed to the Landlord at the same place at which the monthly installment of rent was paid for the month immediately preceding the month in which the right and option to renew is exercised; provided, however, that the amount of the monthly installments of rent shall be determined as provided below in Paragraph III (2).

III.

And the Landlord and Tenant do hereby mutually covenant and agree as follows:

(1) That during the three (3) full calendar months immediately preceding the twentieth (20th), fortieth (40th), sixtieth (60th) and eightieth (80th) anniversaries of the commencement of the term herein granted, the Landlord and Tenant shall agree upon the amount of the monthly installments of rent to be paid during the term ending twenty (20) (or, in the ultimate period, nineteen (19)) years of the term, and in the event they are unable to agree upon the amount of such installments within the first of such three (3) full calendar

months preceding such anniversary, then each shall nominate a qualified real estate expert or appraiser duly licensed as a real estate broker by the Government of the District of Columbia, of reputable standing, who shall have continuously practiced as a licensed real estate broker or appraiser for at least fifteen (15) years, and these two shall nominate a third similarly qualified real estate broker or appraiser, and these three shall agree upon the amount of rent to be paid for the ensuing twenty (20) (or nineteen (19)) year period, such rent to be the fair rental value of the demised land as vacant, unimproved and unoccupied, without regard to the impropriety ascertained by the Tenant at the commencement of the term hereof and without regard to the amount of rent reserved during the initial twenty (20) years of the term hereof, which agreement shall be binding upon the Landlord and the Tenant, and the Landlord and the Tenant do hereby agree to such rent, and agree to share equally the fees of such appraisers; provided, however, that in no event shall the monthly installments of rent during the term hereof exceed be less than Eight hundred, Thirty Three Dollars and Thirty-four cents (\$833.34), except as may be determined by the provisions of Paragraph III (5), below.

(2) That if the Tenant fails to pay any of the said monthly installments of rent in advance as aforesaid, although there shall have been no legal or formal demand made, or if

the Tenant breaks any of the covenants, agreements or conditions herein, then and in any of such events, this agreement and all things herein contained shall, at the option of the Landlord, cease and determine and shall operate as a Notice to Quit, and the Landlord may proceed to recover possession of the demised land under and by virtue of the Code of Laws of the District of Columbia, or by such legal process as may then be in force and effect in like cases relating to proceedings between Landlords and tenants, and when such possession is obtained, the Landlord may resell the demised land at the risk and cost of the defaulting Tenant, whose default, in no event, shall relieve the Tenant of liability for the difference between the rent herein reserved and the rent actually received by the Landlord during the period of the terms herein granted remaining after such default occurs; provided, however, that in the case of a breach of any such covenant, agreement or condition, the Landlord shall give written notice to the Tenant of such breach and shall notify in writing any trustee or trustees or mortgagees or mortgagees of the household estate of such breach and shall allow any person or persons or corporation whose debt is secured by assignment in trust or mortgage of the household estate or any trustee or trustees or mortgagees or mortgagees of the Tenant sixty (60) days from date of such notice within which to effect a cure of such breach; provided, however, that to the extent that a cure of such breach requires

the doing of work, no default shall be declared if within the period of sixty (60) days from the date of such notice such work is begun and thereafter diligently prosecuted; and provided, further, that if such mortgagee or mortgagees or trustee or trustees within the period of thirty (60) days from the date of such notice commence foreclosure proceedings and diligently prosecute such proceedings, no default shall be declared before completion of such foreclosure proceedings; and provided, further, that if the default results from the non-payment of rent, the Tenant shall have seven (7) days from the date of such notice within which to pay the rent; and provided further that, in no event, shall this lease cease and determine for any such breach, the cure of which is beyond the control of the Tenant, Mortgagee or Trustee.

(3) If proceedings shall at any time be commenced for recovery of possession by the Landlord as aforesaid and a compromise or settlement shall be effected, either before or after judgment, whereby the Tenant shall be permitted to retain possession of the demised land, then such proceedings and settlement shall not constitute a waiver of any covenant, condition or agreement contained herein or of any subsequent breach thereof or of this agreement, and the lease shall continue in force according to the terms hereof and the Tenant will perform all of the terms and covenants on its part to be performed.

(4) That, if the whole of the demised land shall be taken or condemned under the exercise of the right of eminent domain by any competent authority, then and in that event, this lease shall cease and determine from the date when possession of the land so taken shall be acquired by the authorities so taking, and the Landlord's interest in the total compensation paid for the demised land and improvements so taken shall be that part of the total award which is allocated to the ground, less the then fair market value of the leasehold estate, and if the award is not allocated between land and improvements and the Landlord and the Tenant are unable to agree upon the Landlord's share of the award, then each shall nominate a qualified real estate expert or appraiser duly licensed as a real estate broker by the Government of the District of Columbia, of reputable standing, who shall have continuously practiced as a licensed real estate broker or appraiser for at least fifteen (15) years, and these two shall nominate a third similarly qualified real estate broker or appraiser, and these three shall agree upon the amount of the award to be allocated to the Landlord and the Tenant, and the Landlord and the Tenant agree hereby to divide the award in such proportions, and to share equally the fees of the said brokers or appraisers.

(5) That if a part of the demised land shall be so taken or condemned by any competent authority, as aforesaid, the compensation received shall first be used for restoration of

the premises to a unit, and the Landlord and the Tenant agree hereby to divide the balance of the award in proportions determined as provided in Paragraph (4) immediately preceding, and the Landlord and the Tenant hereby agree to a reduction in the monthly installments of rent in an amount agreed upon by the said three brokers or appraisers based upon the reduction in the value of the leasehold interest resulting from such partial taking or condemnation.

(6) That all of the covenants, conditions, agreements, rights, privileges, obligations, duties, specifications and recitals herein contained shall be construed as covenants running with the demised land at all times and hereafter binding the heirs, executors, administrators, successors, sub-lessees and assignees of the Landlord and the Tenant, to the end that this lease shall also bind the owner and owners of the fee in the demised land and the owner and owners of the leasehold created hereunder, and that no waiver of any breach of any covenant, condition, or agreement contained herein shall be construed to be a waiver of that condition or agreement or of any subsequent breach thereof or of this agreement.

(7) That this lease shall be conditioned upon the written consent thereto by the Duncan Memorial Methodist Episcopal Church of Danville, Virginia, and the Grace Episcopal Church of Danville, Virginia, consideration under the will of Philip G. Taftlock, deceased, and the Children's Hospital of Washington,

D. C., the contingent remainderman under the Will of Philip G. Affleck, Deceased, and that such consent shall be evidenced by attachment hereto of a resolution or other official record of action of the governing body of such remainderman, authorizing an appropriate official to sign such consent hereinbelow, and by the signature and seal of such official; and, further, that this lease shall be conditioned upon issuance of a certificate by a real estate title company evidencing title to the fee in the landlord and an opinion from such title company favoring the validity of this lease under the terms of the Will of Philip G. Affleck, Deceased.

In witness whereof the parties hereto have signed their names and affixed their seals this day and year hereinbefore written.

WITNESSES:

John J. Barrett McDonnell Grace B. Affleck (SPW)
Landlord

John J. Barrett McDonnell John H. Polkherne (SPW)
Landlord

WITNESSES:

John J. Ferguson
see to all three

Frederick Ring (SPW)
Tenant

Mary J. Ring (SPW)
Tenant

Carlyle P. Cohen (SPW)
Tenant

APPROVED:

WITNESSED:

W. J. McLean, Jr. (S.W.)
 Vice-Chairman, Mineral Randolph
 County of Roanoke, Virginia.

W. J. Gilbert McLean (S.W.)
 Vice-President, First Methodist Church of
 Roanoke, Virginia.

John E. Hanson
W. J. Hanson, Chairman (S.W.)
 Vice-Chairman, Children's Hospital
 of Washington, D. C.

W. H. J. Potts

W. Frances G. Cooke

W. Dan C. Parker

DESCRIPTION OF DOCUMENT, TO WIT:

I, Wifay B. Braggle, a Notary Public
 in and for the District of Columbia, DO HEREBY CERTIFY that
 Grace B. Affleck and John H. Polkifhorn, parties to a certain
 Lease Agreement, bearing date on the 28th day of September,
 1960, and hereto annexed, personally appeared before me in said
 District, the said Grace B. Affleck and John H. Polkifhorn being
 personally well known to me as the persons who executed the said
 Lease Agreement, and acknowledged the same to be their act and
 deed.

Subscribed under my hand and seal this 28th day of September,
 1960.

Wifay B. Braggle (S.W.)
 Notary Public, D. C.

[Caption Omitted in Printing]

STIPULATION

It is hereby stipulated and agreed by counsel for both parties in the above-entitled action as follows:

1. Philip G. Affleck, the Testator and Grantor of the Testamentary Trusts involved herein, died January 7, 1947. At the time of his death his sole business and occupation was the ownership and management of rental real estate.

2. After several specific bequests, the will of Philip G. Affleck (a copy of which is attached hereto and marked Exhibit A) bequeathed and devised his estate, consisting principally of real estate, to his wife, Grace B. Affleck, for her life, subject only to proper maintenance of the real estate, payment of taxes thereon, and payment of interest on existing or future encumbrances on such real estate. In the event of sale by her of real estate with the approval of the testamentary trustee, proceeds of such sale were to be invested in District of Columbia real estate.

3. Under the will, at the death of Grace Affleck the estate was devised to the trustee for the benefit of two life income beneficiaries and their issue, if any, until such issue reached the age of 21, and thereafter the remainder was vested in two churches located in Berryville, Virginia.

4. The estate consisted principally of real estate, most of which was encumbered to secure indebtedness at the date of death of Philip G. Affleck.

5. Included in the estate was investment real estate, now identified as Lots 833 and 868 in Square 140 in the District of Columbia, which was encumbered in September, 1960, by a loan of \$27,500.00.

6. In September, 1960, the life tenant and the trustee, with consent of the vested remaindermen, entered into a 99-year lease (a copy of which is attached to the deposition of J. Henry Polkinhorn and marked Government Exhibit 1) of the real estate in question, electing a minimum rental of \$10,000 per year on the property as encumbered. In the negotiation of the lease, the lessee offered a minimum rental of \$12,000 per year for the property if unencumbered by a loan, or, alternatively, a minimum rental of \$10,000 per year for the property if encumbered.

7. The lease provided that, as part of and in reduction of the total rental to be paid, the lessee would assume the lessor's obligations for payment of principal and interest on the indebtedness and would discharge the indebtedness before razing the improvements then standing on the property at the commencement of the lease, which improvements were declared by the lease to be the property of the lessee.

8. In October or November, 1960, the lessee paid the existing \$27,500 indebtedness and all accrued interest and did raze the existing building and thereafter erected on the property a building containing elevators and other facilities for offices in the lessee's building standing on the adjacent land.

9. Grace B. Affleck timely filed her individual federal income tax return, Form 1040, for the year 1960 (a copy of which is attached hereto and marked Exhibit B), showing no tax due thereon.

10. Thereafter, a timely assessment was made by the Internal Revenue Service against Grace B. Affleck in the total amount of \$10,112.33 representing deficiency in tax of \$8,802.68 and assessed interest of \$1,309.65 resulting from the inclusion of \$27,500.00 as

ordinary income to her in the year 1960 and other adjustments not here in dispute.

11. The total amount of the deficiency assessment was paid to the defendant on October 8, 1963.

12. Thereafter, a timely claim for refund, in the amount of \$10,096.41 was filed on November 7, 1963, together with Form 982 in duplicate and statement attached thereto (a copy of which is attached hereto and marked Exhibit C) and a letter of explanation from Grace B. Affleck (a copy of which is attached hereto and marked Exhibit D).

13. The claim for refund was formally rejected by statutory notice of disallowance dated November 4, 1964.

14. Thereafter, this suit was timely filed by J. Henry Polkinhorn, the duly appointed, qualified and acting Executor of the Estate of Grace B. Affleck, deceased, who died a resident of the District of Columbia on June 20, 1964, and John H. Polkinhorn (who is the same individual as plaintiff J. Henry Polkinhorn), the duly appointed, qualified and acting Trustee of the Testamentary Trust established by the will of Philip G. Affleck, deceased.

15. The two issues for determination in this case are as follows:

a. Whether the Court has jurisdiction over this action with respect to the plaintiff John H. Polkinhorn, Trustee of the Testamentary Trust established by the will of Philip G. Affleck, deceased; and,

b. whether Grace B. Affleck received taxable ordinary income in the amount of \$27,500.00 in the year 1960, as the Government contends, or whether such income is excludable under Section 108 of the Internal Revenue Code of 1954, as the

plaintiffs contend, or, if such amount was income whether it was income to the trust and permanently set aside for the charitable remaindermen as is alternatively contended by the plaintiffs.

16. The following documents attached hereto and made a part hereof are true and correct copies of the originals thereof and no objection will be raised by either party as to their authenticity:

- a. Exhibit A -- Will of Philip G. Affleck
- b. Exhibit B -- Form 1040, federal income tax return of Grace B. Affleck for the calendar year 1960.
- c. Exhibit C -- Form 982 and attached statement filed with the Internal Revenue Service by Grace B. Affleck.
- d. Exhibit D -- letter of explanation to Internal Revenue Service from Grace B. Affleck.

W. B. McDonnell
 W. Barrett McDonnell, Esquire
 Suite 430
 Washington Building
 Washington, D. C. 20005
 Counsel for Plaintiffs


 Daniel L. Penner
 Attorney
 Department of Justice
 Tax Division
 Washington, D. C. 20530
 Counsel for Defendant

[Exhibit A]

LAST WILL AND TESTAMENT OF
PHILIP G. AFFLECK

I, PHILIP G. AFFLECK, of the District of Columbia, do make, publish and declare this instrument of writing as and for my last will and testament, intending hereby to dispose of all the estate in which I may be interested in any manner at the time of my death, and I do hereby revoke any and all wills, testaments and codicils heretofore at any time by me made.

ITEM I: I will provide by insurance for the immediate requirements of my wife GRACE B. AFFLECK, to whom I give and bequeath my automobile, my household furniture, furnishings, bric-a-brac and other personal effects (other than securities) which shall be within my residence or living apartments and instorage, at the time of my death.

ITEM II: I bequeath to JOHN R. BELLER, of the District of Columbia, the sum of One thousand dollars (\$1,000) if he is in my employ at the time of my death, otherwise this bequest shall lapse.

ITEM III: All the rest, residue and remainder of my estate I give, devise and bequeath to my wife Grace B. Affleck, TO HAVE AND TO HOLD, for and during her natural life, subject only to the proper maintenance of the real estate held under the terms of this instrument, the payment of all taxes and assessments levied thereon from time to time, and the payment of all interest on existing or future encumbrances on such properties or any thereof. I authorize and empower my said wife, with the consent and approval of my trustee hereinafter named, to sell and convey any or all of said real estate. In the event of any sale or sales of real estate the proceeds thereof are to be reinvested in real estate in the

District of Columbia which shall be approved by said trustee and which shall thereafter be held upon the trusts hereby created.

It is my wish that out of the income arising from the property so bequeathed and devised to my said wife she shall make provision for my daughter Marian should the latter need help or assistance during the lifetime of my wife.

ITEM IV: Upon the death of my said wife I give, devise and bequeath all the rest, residue and remainder of my estate to BARNUM L. COLTON, now vice-president of the National Savings and Trust Company, in and upon the following trusts, that is to say; IN TRUST:

(a) To manage, control, rent, sell, exchange, transfer, convey and encumber by deed of trust or otherwise, all or any part of the trust estate created by this instrument, in fee simple or in any lesser estate, with the power of investment and reinvestment, and to change and alter such investments from time to time, to collect all rents, revenue and income arising therefrom and to pay such costs, charges and expenses as may be necessary or proper in the administration thereof apportioning such costs, charges and expenses between the principal and income of said trust estate as he may deem right and proper.

(b) To pay to my daughter MARIAN AFFLECK one-half of the net income arising from said trust estate for and during her natural life, and upon her death leaving issue her surviving, to pay said one-half of said net income to such issue, or apply the same for their respective maintenance, support and education until they each respectively shall arrive at the age of twenty-one (21) years. Upon the death of my said daughter leaving no issue her surviving to thereafter pay all the net income arising from said trust estate to my stepson JOHN H. POLKINHORN for and during his natural life.

(c) To pay the other half of said net income to the said JOHN H. POLKINHORN for and during his natural life, and upon his death leaving issue his surviving, to pay twenty-five (25) percentum of the one-half of said net income so left for his use and benefit, toward the support, education and maintenance of his children until they shall have respectively arrived at the age of maturity, and the remaining seventy-five (75) percentum thereof to my said daughter, or in the event of her prior decease leaving issue her surviving, to apply the same to the support, education and maintenance of such issue until they shall respectively arrive at said ages. Upon the death of the said John H. Polkinhorn leaving no issue him surviving, my said daughter or her issue surviving him, to pay to my said daughter during her lifetime all of said income, and after her death pay the same for the maintenance, support and education of her issue until they severally arrive at the age of maturity.

(d) Upon the death of my said daughter leaving no issue her surviving and the death of the said John H. Polkinhorn leaving no issue him surviving, or if both or either of them leave issue her or him surviving, upon the death of all of such issue, or their all arriving at the age of maturity, to pay over the entire principal of said trust estate then existing, together with all unexpended income therefrom to the DUNCAN MEMORIAL M.E. CHURCH and to the GRACE EPISCOPAL CHURCH, both of Berryville, Virginia, in equal parts, absolutely and in fee simple.

ITEM V: Should my said wife predecease me, or should she survive me but not be living at the time for the completion of the administration of my personal estate, I bequeath the sum of Five thousand dollars (\$5000) to WHARTON E. LESTER if he then be living, or in the event of his prior death, to such of his daughters as may then be living, in equal

shares, or the whole to the survivor thereof. This bequest is made in consideration of the friendship I have for Mr. Lester as a token of appreciation for his services in assisting me to accumulate what I have and because I am indebted to him for legal services he has heretofore rendered me an amount much greater than said sum, for which services I have never felt in a position to pay and the payment thereof may otherwise be barred by time. This bequest shall not include any current indebtedness I may owe him at the time of my death and shall not be in lieu of compensation to him for acting as executor under this instrument. If my said wife survives me I direct the payment of the said \$5000 to be made upon her death.

ITEM VI: Should my wife, daughter and stepson all predecease me, my daughter and stepson leaving no issue them surviving, I give, devise and bequeath my entire estate then remaining after the payment of said bequest of \$5000, to the Duncan Memorial M. E. Church and the Grace Episcopal Church, of Berryville, Virginia aforesaid, in equal parts, absolutely and in fee simple.

ITEM VII: My said wife and my said trustee are each hereby given full power and authority to renew, replace or pay any encumbrance secured upon any real estate I may own at the time of my death and to execute such deed or deeds or other instruments as may be required. To enable them to properly administer the trusts hereby created I authorize and empower them and each of them to execute such deed or deeds as may be necessary or proper, and hereby relieve any and all purchasers and any and all lenders of money secured on any such property from seeing to the application of the purchase money or money loaned.

ITEM VIII: I charge my executors and my trustee hereinafter named to notify the respective ministers in charge of the Duncan Memorial M.E.

Church, and the Grace Episcopal Church aforesaid, or the trustees managing the affairs of said churches, at or shortly after my death, of the benefits the said institutions and each thereof may ultimately receive under this instrument if they are capable of receiving bequests or devises, to the end that they and each thereof, if not already incorporated, may become incorporated (if that be necessary), and receive the property herein bequeathed and devised to them respectively. In the event that but one of said churches is capable of taking and holding property hereunder that one shall receive all the benefits devised and bequeathed to both thereof, and if neither of them have such authority, or if for any reason neither of them may receive the benefits intended for them by this instrument, then in such event I give, devise and bequeath all left herein for the benefit of said churches to the CHILDREN'S HOSPITAL OF WASHINGTON, D.C.

It is my desire that each of said churches shall use so much of the funds it shall receive hereunder, as in the judgment of its governing authorities is right and advisable, for the maintenance of its Sunday School as memorials to my deceased father.

ITEM IX: Mindful that estate, inheritance and possibly other taxes will be payable upon my death, that my estate will probably consist principally of real estate, and desiring that such real estate be preserved as far as possible for the purposes set forth in my said will, I hereby authorize and empower my personal representative or representatives acting under this instrument to borrow such sum or sums of money upon the security of any parcel or parcels of real estate I may own at the time of my death that may be required for the purpose of paying such taxes or any part of any thereof, upon such terms and conditions as may be necessary or advisable, and as security therefor to execute such deed or

deeds of trust, note or notes and other instruments as may be necessary, advisable or proper, and apply the proceeds of any such loan or loans to the payment of such taxes or any part thereof, the lender or lenders of the money being hereby relieved from seeing to the application thereof.

I direct that the interest on any such sum or sums so borrowed shall be paid primarily from the income arising from the real estate upon which the indebtedness shall be secured but if such income at any time be insufficient for that purpose, that such interest be paid by the life tenants or tenant of other real estate held under the terms of this instrument, but shall not become an encumbrance or lien on any other real estate so held.

ITEM X: In the event of the death of the said Barnum L. Colton prior to the execution of the trusts in him reposed I request my said wife, or in the event of her death, the said John H. Polkinhorn to apply to the court for the appointment of a trustee in the place and stead of the said Barnum L. Colton.

ITEM XI: I nominate and appoint my said wife, GRACE B. AFFLECK, as executrix, and WHARTON E. LESTER as executor of this instrument and request that neither thereof be required to give bond or undertaking in connection therewith. In the event that the said Wharton E. Lester shall predecease me or die before this will has been admitted to

probate and record I appoint the said BARNUM L. COLTON as co-executor in his place and stead.

IN WITNESS WHEREOF I have hereunto set my hand and seal this 23rd day of May, A.D. 1944.

/s/ PHILIP G. AFFLECK (Seal)

SIGNED, SEALED, PUBLISHED and DECLARED by the above-named testator, PHILIP G. AFFLECK, and as for his last will and testament, in our presence, who at his request, in his presence and in the presence of each other have hereunto signed our names as witnesses thereto this 23rd day of May, A.D. 1944.

/s/ GRACE TAYLOR Address: 1117 Vt. Ave., N.W., Wash., D.C.

/s/ CROOM W. WALKER Address: Claridge Hotel, 820 Conn., Ave.

Form 1040-1960 EXEMPTIONS FOR PERSONS OTHER THAN YOUR WIFE AND CHILDREN

Page

Name	Relationship	Months lived in your home, if born or died during year also write "B" or "D"	Did dependent have gross income of \$500 or more?	Amount YOU furnished for dependent's support, if 100% write "All"	Amount furnished by OTHERS including dependent (See instructions, p. 4)
				\$	\$

Enter on line 3, page 1, the number of exemptions claimed above.

⇒ If an exemption is based on a multi-lateral agreement of a group of persons, attach the declarations described on page 5 of instructions.

ITEMIZED DEDUCTIONS—IF YOU DO NOT USE TAX TABLE OR STANDARD DEDUCTION

If Husband and Wife (Not Legally Separated) File Separate Returns and one Marries Deductions, the Other Must Also Itemize

State to whom paid. If necessary, write more than one item on a line or attach additional sheets. Please put your name and address on any attachments.

Contributions	See Attached Schedule			\$ 206 16
	Total paid but not to exceed 20% of line 11, page 1, except as described on page 8 of instructions....			
Interest			Total interest	-- --
	Real estate taxes.....	State income taxes.....	\$88.00	
Taxes	State and local sales taxes.....	Other taxes (specify).....		136 00
			Total taxes:	
Medical and dental expense (Submit itemized list. Do not enter any expense compensated by insurance or otherwise)	NOTE: If you or your wife are 65 years of age or over, or if you or your wife is a dependent parent 65 or over, do not use this schedule. See page 9 of the instructions for larger deduction. Continue use schedule below.			2,571
	1. Total cost of medicine and drugs.....		\$ 256 39	
Other Deductions (See page 10 of Instructions and attach information required)	2. 1 percent of line 1, page 1. Non-business income.....		6 87	7
	3. Excess, if any, of line 1 over line 2.....		249 52	
	4. Other medical and dental expenses.....		2,322 10	2,921
	5. Total of lines 3 and 4.....		2,571 62	
	6. Enter 3 percent of line 11, page 1.....		\$ over 65	2,921
	7. Allowable amount (excess of line 5 over line 6; see page 10 for maximum limitation).....		\$ 7.50	
	Safe Deposit Rental.....			2,921
			Total	

TOTAL DEDUCTIONS (Enter here and on line 2 of Tax Computation, below).....

\$ 2,921

TAX COMPUTATION—IF YOU DO NOT USE THE TAX TABLE

1. Enter Adjusted Gross Income from line 11, page 1.....	\$ (1,210
2. If deductions are itemized above, enter total of such deductions. If deductions are not itemized and line 1, above, is \$5,000 or more, enter the smaller of 10 percent of line 1 or \$1,000 (\$500 if a married person filing a separate return).....	2,921
3. Balance (line 1 less line 2).....	(4,131
4. Multiply \$600 by total number of exemptions claimed on line 4, page 1.....	1,200
5. Taxable Income (line 3 less line 4).....	(5,331 54)
6. Tax on amount on line 5. Use appropriate tax rate schedule on page 15 of instructions. Do not use Tax Table on page 16.....	None
7. If you had capital gains and the alternative tax applies, enter the tax from separate Schedule D.....	
8. Tax credits. If you itemized deductions, enter:	
(a) Credit for income tax payments to a foreign country or U.S. possession (Attach Form 1116).....	\$
(b) Tax paid at source on tax-free covenant bond interest and credit for partially tax-exempt interest.....	
(c) Total.....	Enter here →
9. Enter here and on line 12, page 1, the amount shown on line 6 or 7 less amount claimed on line 8(c)....	\$ None

1960

Form 1040

Page 2

Grace B. Affleck
2737 Devonshire Place, N.W.
Washington 8, D.C.

CONTRIBUTIONS

Exempt Contributions:

*Pilgrim Lutheran Church	\$344.00		
*National Lutheran Home	30.00		
National Society for the			
Prevention of Blindness	30.00		
*Mount Vernon Seminary	15.00		
*National Health Foundations	<u>15.00</u>	\$434.00	
10% of Non-Business Income		<u>68.72</u>	\$68.72
Balance			\$365.28

Other Contributions:

*Soldiers, Sailors, Marines and			
Airmens Club	<u>2.00</u>		
Total	\$367.28		
20% of Non-Business Income	<u>137.44</u>		<u>137.44</u>
Non-Deductible Contributions		\$229.84	
Deductible Contributions			<u>\$206.16</u>
<u>*Total for District of Columbia Return</u>			<u>\$406.00</u>

Grace B. Affleck
 2737 Devonshire Place, N.W.
 Washington 8, D.C.

1960
 Form 1040
 Page 2

MEDICAL AND DENTAL EXPENSE

Professional Fees:

Harvey Lee Cloud, M.D.	\$490.00
Sterling Bookoven, M.D.	10.00
J. Burton Glenn, M.D.	130.00
Groover, Christie & Merritt	250.00
Holtzman & Wechsler	15.00
Oscar B. Hunter Memorial Laboratory	<u>7.00</u>
	\$902.00

Doctors Hospital	866.60
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Nurses	522.00
--------	--------

Optical	<u>31.50</u>
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Total for Federal Return	<u>\$2,322.10</u>
--------------------------	-------------------

Medicines and Drugs	<u>256.39</u>
---------------------	---------------

Total for District of Columbia Return	<u>\$2,578.49</u>
--	-------------------

U. S. Treasury Department—Internal Revenue Service
GAINS AND LOSSES FROM SALES OR EXCHANGES OF PROPERTY
Attach this schedule to your Income Tax Return, Form 1040

Non-^a and ^b values as shown on page 1 of Form 1040

Grace S. Affleck, 2737 Devonshire Place, N.W., Washington 8, D.C.

(1) CAPITAL ASSETS

Short-Term Capital Gains and Losses—Assets Held Not More Than 6 Months

2. Enter your share of net short-term gain (or loss) from partnerships and fiduciaries.....
3. Enter unused capital loss carryover from 5 preceding taxable years (Attach statement!).....
4. Net short-term gain (or loss) from lines 1, 2, and 3..... \$2,000.00

Long-Term Capital Gains and Losses—Assets Held More Than 6 Months

- | | |
|---|--------------|
| 6. Enter the full amount of your share of net long-term gain (or loss) from partnerships and S corporations..... | S ----- |
| 7. Net long-term gain (or loss) from lines 5 and 6..... | \$ 23,000.00 |
| 8. Combine the amounts shown on lines 6 and 7, and enter the net gain (or loss) here..... | ----- |
| 9. If line 8 shows a GAIN—Enter 50 percent of line 7 or 50 percent of line 8, whichever is smaller. (Enter zero if there is a loss or no entry on line 7)..... | ----- |
| 10. Deduct line 9 from line 8. Enter balance here and on line 1, Schedule D Summary on page 3 of Form 1040..... | S ----- |
| 11. If line 8 shows a LOSS—Enter here and on line 1, Schedule D Summary, Form 1040, the smallest of the following:
(a) the amount on line 8; (b) taxable income computed without regard to capital gains and losses and the deduction for charitable gift; or (c) \$1,000..... | S ----- |

COMPUTATION OF ALTERNATIVE TAX.—Use only if the net long-term capital gain exceeds the net short-term capital loss, or if there is a net long-term capital gain only, and you are filing (a) a separate return with taxable income exceeding \$18,000, or (b) a joint return or as a surviving husband or wife, with taxable income exceeding \$33,000, or (c) as a head of household with taxable income exceeding \$24,000.

12. Enter the amount from line 5, page 2, of Form 1040	\$.....
13. Enter amount from line 9 above.....
14. Balance (line 12 less line 13).....	\$.....
15. Enter tax on amount on line 14 (Use applicable tax rate schedule on page 15 of Form 1040 Instructions)	\$.....
16. Enter 50 percent of line 13.....
17. Alternative tax (line 15 plus line 16). If smaller than amount on line 6, page 2, Form 1040, enter this alternative tax on line 7, page 2, Form 1040	\$.....

ALL PROPERTY OTHER THAN CAPITAL ASSETS

Grace. B. Affleck
2737 Devonshire Place, N.W.
Washington 8, D.C.

1960
Form 1040
Net Operating Loss

Non-Business Deduction Modification

Non-Business Gross Income	\$ 687.19
Non-Business Deductions	<u>2,921.28</u>
Excess Deductions	<u>\$2,234.09</u>

Net Operating Loss Computation

1. Income Tax Net Loss	\$5,331.94
2. Net Operating Loss Deduction	None
3. Capital Gain and Loss Modification	None
4. Personal Exemptions on Return	\$1,200.00
5. Non-Business Deduction Modification	<u>2,234.09</u>
6. Total	<u>3,434.09</u>
7. Net Operating Loss	<u>\$1,897.85</u>

Exhibit C

FORM 932 REV. DEC. 1953	U. S. TREASURY DEPARTMENT - INTERNAL REVENUE SERVICE
CONSENT OF TAXPAYER TO ADJUSTMENT OF BASIS OF PROPERTY UNDER SECTION 1017 OF THE INTERNAL REVENUE CODE OF 1954 (To be executed and filed in duplicate)	
Grace B. Affleck 579-60-3022. <small>(Name)</small>	
2737 Devonshire Place, N.W. Washington, D.C. <small>(Address)</small>	
has excluded under section 103(c) of the Internal Revenue Code the amount of \$27,500.00 from gross income for the taxable year beginning <u>January 1, 1960</u> , and ending <u>December 31, 1960</u> : Under that section such taxpayer consents to have the basis of property adjusted in accordance with the regulations prescribed under section 1017 of the Internal Revenue Code of 1954, in effect at the time of filing the taxpayer's return for that year, or amended return or claim for credit or refund. The taxpayer's principal office or place of business but resides <u>2737 Devonshire Place, N.W., Washington, D.C.</u> <small>(Number and street, post office, State)</small>	
On <u>October 10</u> 19 <u>60</u> a discharge of indebtedness was obtained for which indebtedness the taxpayer was liable or subject to which the taxpayer held property. <u>Grace B. Affleck</u> <small>(Signature of taxpayer)</small>	
<u>10-31-63</u> <small>(Date)</small>	
APPROVED: <u>John H. Polkinhorn</u> <small>(Signature)</small> (John H. Polkinhorn, Trustee of the Testamentary Trusts established by the Will of Philip G. Affleck, Deceased. <small>(Title)</small>	
<u>10-31-63</u> <small>(Date)</small>	

 CORPORATE
SEAL

INSTRUCTIONS

- (1) This form is to be used by a taxpayer excluding from gross income any amounts of income attributable to the discharge, within the taxable year, of the indebtedness of which the taxpayer is liable or subject to which the taxpayer holds property.
- (2) This form should be executed in duplicate and filed with the return or with an amended return or claim for credit or refund, as the case may be.
- (3) The consent shall be signed by the taxpayer. If the taxpayer is a corporation, the consent shall be signed with the corporate name followed by the signature and title of an officer of the corporation empowered to sign for the corporation, in addition to which the corporate seal must be affixed. If the corporation has no seal, the consent must be accompanied by a certified copy of the resolution passed by the board of directors, giving such officer authority to sign the consent.
- (4) If the taxpayer desires to have the basis of property adjusted in any manner different from the general rule set forth in the regulations, in effect at the time of filing the return, pre-

scribed under section 1017 of the Internal Revenue Code of 1954, the precise method (including allocation of amounts) should be set forth in detail on separate sheets attached to this form. Consent by the Commissioner of Internal Revenue to any departure from such general rule shall be effected only by a closing agreement entered into under the provisions of section 7121 of the Internal Revenue Code of 1954.

(5) The consent filed on this form shall be deemed to be a consent to the application of the general rule set forth in the regulations and such general rule shall prevail in the determination of the basis of the taxpayer's property, unless the taxpayer specifically states on this form or on a separate sheet attached hereto and made a part hereof that the taxpayer does not consent to the application of the general rule.

(6) There shall be attached to this form a complete statement and description of the transactions resulting in discharge of indebtedness covered by this consent and of the nature of such discharge.

Form 1040-1660

Page 3

IF INCOME WAS ALL FROM SALARIES AND WAGES, TEAR OFF THIS PAGE AND FILE ONLY PAGES 1 AND 2

Schedule A.—INCOME FROM DIVIDENDS (Income from Savings (Building) and Loan Associations and Credit Unions should be entered as interest in Schedule B)

1. Name of qualifying corporation declaring dividend (See instructions, page 11): (Indicate by (H), (M), (U) whether stock is held by husband, wife, or jointly)	Amount	
Potomac Electric Power Company	\$ 264.00	
2. Total	\$ 264.00	
3. Exclusion of \$50 (if both husband and wife received dividends, each is entitled to exclude not more than \$50 of his (her) own dividends)	50.00	
4. Excess, if any, of line 2 over line 3. Enter here and on line 1, Schedule J	\$ 214.00	
5. Name of nonqualifying corporation declaring dividend:		
6. Enter total of lines 4 and 5	\$ 214.00	

Schedule B.—INCOME FROM INTEREST (This includes interest credited to your account)

Name of payer	Amount	Name of payer	Amount
Nat. Farm. Sav & Loan	\$ 161.08		\$
Perpetual Bldg. Assn	71.54		
Liberty Sav. & Loan	180.18		
Tax Refunds	60.39		
Enter total here-->			473.19

Schedule C.—SUMMARY OF GAINS AND LOSSES FROM SALES OR EXCHANGES OF PROPERTY

1. From sale or exchange of capital assets (from separate Schedule D)	
2. From sale or exchange of property other than capital assets (from separate Schedule D)	

Schedule E.—INCOME FROM PENSIONS AND ANNUITIES (See instructions, page 12)

Part 1.—General Rule

1. Investment in contract	\$	4. Amount received this year	\$
2. Expected return	\$	5. Amount excludable (line 4 multiplied by line 3)	
3. Percentage of income to be excluded (line 1 divided by line 2)	%	6. Taxable portion (excess of line 4 over line 5)	

Part 2.—Where your employer has contributed all or part of the cost and your contribution will be recovered tax-free within three years. If your cost was fully recovered in prior years, enter the total amount received in line 5 omitting lines 1 through 4.

1. Cost of annuity (amounts you paid)	\$	4. Amount received this year	\$
2. Cost received tax-free in past years			
3. Remainder of cost (line 1 less line 2)	\$	5. Taxable portion (excess, if any, of line 4 over line 3)	

Schedule F.—INCOME FROM RENTS AND ROYALTIES

1. Kind and location of property (Identify whether rent or royalty)	2. Amount of rent or royalty	3. Depreciation (explain in Sch. D) or depletion	4. Repairs (attach itemized list)	5. Other expenses (attach itemized list)
	\$	\$	\$	\$
1. Totals	\$ 53464.65	\$ 55,827.75	\$ 8,435.55	\$ 41099.20
2. Net income (or loss) from rents and royalties (column 2 less sum of columns 3, 4, and 5)				(1,897.85)

Schedule G.—OTHER INCOME OR LOSSES

1. Partnerships (name, address, and nature of income)	
2. Estates or trusts (name and address)	
3. Other sources (state nature)	
Total income (or loss) from above sources (Enter here and on line 10, page 1)	\$ (1,210.66)

570-10-76135-1

[SCHEDULE "G" ILLEGIBLE]

Grace B. Affleck
2737 Devonshire Place, N.W.
Washington 8, D.C.

1960
Form 1040
Schedule I

DEPRECIATION

Description of Asset	Date Acquired	Zasis	Prior Deprec.	Life	Deprec.
1. 1411-11th St. N.W. (Sold 10/21)	1947	\$14,000.00	7,280.00	25 yrs.	\$ 455.01
2. 1725-11th St. N.W.	1947	2,500.00	1,300.00	25 yrs.	100.00
3. 1226-14th St. N.W. " New Furnace	1947 1959	10,500.00 1,900.00	5,460.00 190.00	25 yrs. 10 yrs.	420.00 190.00
4. 2100-14th St. N.W.	1947	27,000.00	10,400.00	25 yrs.	800.00
5. 1826-M St. N.W. (Leased-Razed 10/9)	1947	25,000.00	12,546.50	25 yrs.	807.74
6. 6928 Maple St. N.W.	1947	3,500.00	1,820.00	25 yrs.	140.00
7. 1130 N.H. Ave. N.W. (Sold 3/24)	1947	5,000.00	2,600.00	25 yrs.	50.00
8. 1206-O St. N.W. " New Furnace(1/4 yr.)	1947 10/60	5,000.00 850.00	2,600.00 None	25 yrs. 10 yrs.	200.00 21.00
1209-O St. N.W.	1947	6,000.00	3,120.00	25 yrs.	240.00
9. 1417-1427-P St. N.W.	1947	27,000.00	14,040.00	25 yrs.	1,080.00
10. 2421-23 Pa. Ave. N.W.	1947	10,000.00	5,200.00	25 yrs.	400.00
11. 4010-12 So. Cap. St. (7mo)	6/60	39,576.00	None	25 yrs.	924.00
			Total Depreciation 1960		\$5,827.75

Grace B. Affleck, 579-60-3022
 2737 Devonshire Place, N. W.
 Washington, D. C. 20008

1960 AMENDED
 FORM 1040
 Form 982

STATEMENT AND DESCRIPTION OF THE TRANSACTIONS
 RESULTING IN DISCHARGE OF INDEBTEDNESS AND THE
 NATURE OF SUCH DISCHARGE

Under the Will of Philip G. Affleck, deceased; who died January 7, 1947, the Taxpayer holds title as life tenant to certain real estate located in the District of Columbia, all of which is used by her for the production of income in the form of rents. At the death of the Taxpayer, the said estate passes into a trust for the joint lives of John H. Polkinhorn and Marian G. Affleck, and at the death of the survivor of them without issue or after their deaths when the last of their issue attains the age of 21 years, the said estate passes in fee simple to the Duncan Memorial Methodist Episcopal Church and the Grace Episcopal Church, both of Berryville, Virginia, or, in the event these vested remaindermen cannot take title to the property at that time, then to the Childrens Hospital of the District of Columbia.

Included in said real estate is a parcel designated for purposes of District of Columbia real estate property tax as Lots 833 and 868 in Square 140, originally improved by the premises known as 1826 M Street, N. W.

The said property, together with the improvements thereon, was valued at \$37,500.00 in the final adjustment of the United States estate tax return for the estate of Philip G. Affleck, deceased. The adjusted basis, as of January 1, 1960, was as follows:

Market value at date of inheritance,	\$37,500.00
Depreciation allowed or allowable, 1947 to 1959, inclusive,	12,546.50
Adjusted basis,	<u>\$24,953.50</u>

On September 28, 1960, the Taxpayer and the testamentary Trustee of the Estate, with the approval of the two vested remaindermen churches and the contingent remainderman hospital, entered into a lease of the said property for a term of 99 years to Gustave Ring, Marion L. Ring, and Carlyn Ring Cohen, at a minimum monthly rental of \$833.34, subject to renegotiation at 20-year intervals during the life of the lease.

As a condition of the lease and as part of the total consideration therefor, the lessees were given title to the improvements standing on the property with the right to raze said improvements, provided they first discharged the existing loan of \$27,500.00 on the said property, secured by a first deed of trust. The lessees did discharge the said indebtedness on or about October 10, 1960, and did raze the building standing thereon which secured the loan.

The foregoing facts, together with copies of the Will of Philip G. Affleck, deceased, and of the said lease agreement, have been submitted to the Audit and Appellate Divisions of the Internal Revenue Service in connection with the audit of the Taxpayer's individual income tax return for 1960 and the appeal from the proposed adjustments thereto.

Under Section 108(a) of the Internal Revenue Code of 1954, as amended, and the regulations issued thereunder, the Taxpayer has excluded from her gross income the \$27,500.00 payment to the holders of the notes secured by the First Deed of Trust in discharge of the indebtedness assumed by the said lessees. Since the property was held subject to the indebtedness, and the indebtedness was incurred or assumed by the taxpayer, and individual, in connection with property used in her trade or business, she is entitled to consent to adjustment of the basis of the property under Section 1017 of the Internal Revenue Code of 1954.

Exhibit D

October 31, 1963.

District Director
Internal Revenue Service
Baltimore 2, Maryland

Re: Grace B. Affleck,
2737 Devonshire Place, N. W.
Washington 20008, D. C.
ORIG OE 1929 61 L 1040 ADDL
60 D 140814
Individual Income Tax 1960, AMENDED

Dear Sir:

My individual income tax return, Form 1040, for the calendar year 1960 is hereby amended as follows:

I consent to adjustment of the basis of income-producing property owned by me as life tenant under Section 1017 of the Internal Revenue Code of 1954 and incorporate into my said income tax return the attached Form 982, together with the statement attached thereto.

In this connection your attention is directed to the deficiency in income tax for the year 1960, assessed against me in the amount of \$8802.68, paid with interest by me, and received at your office October 8, 1963.

Simultaneously herewith, I am filing a claim for refund of income tax erroneously assessed by failure of the Internal Revenue Service to apply Section 108(a) of the Internal Revenue Code of 1954, as amended, to the transaction described in the attached statement.

You are requested to accept this Amendment and the attached Consent, which was not filed with the original return because the alleged income did not appear in the record of my cash receipts and disbursements from which my Form 1040 was prepared and was, therefore, overlooked by the Preparer. Thereafter, amendment was postponed at the request of Audit during examination of the Return.

Very truly yours,

Grace B. Affleck
Grace B. Affleck

[Caption Omitted in Printing]

FILED

DEC 17 1968

ROBERT M. STEARNS, Clerk

Corrected copy
of oral opinion
delivered from the
bench, December 4, 1968

OPINION

W. Barrett McDonnell, of Washington, D. C., on
behalf of the plaintiffs.

Daniel L. Penner, Department of Justice, Washington,
D. C., on behalf of the defendant.

This is an action for a refund of income taxes
claimed to have been erroneously assessed and paid. The
action involves the interpretation and application of
Section 108 of the Internal Revenue Code, 26 U.S.C. §108.

The case has been submitted to the Court on a stipu-
lation of facts. Philip G. Affleck, who died on January 7,
1947, created a trust estate by his will, under which his
wife, Grace B. Affleck was the life tenant. A part of the
estate was a parcel of improved real property in the
District of Columbia, encumbered by a mortgage of \$27,500.
In September 1960, the life tenant and the trustee made a
99-year-lease of this property. In addition to paying a

rent of \$10,000 a year, the lessee by terms of the lease assumed the lessor's obligation of the payment of principal and interest on the indebtedness, and in case the lessee decided to demolish the building, he was to discharge the entire indebtedness before doing so. In the fall of 1960 the lessee paid off the entire indebtedness of \$27,500 and then demolished the building situated on the property. The Internal Revenue Service, claiming that this payment of \$27,500 was income to the life tenant, Grace B. Affleck, assessed her in the total amount of \$10,112.33, which represented a deficiency in her income tax on the theory that the sum of \$27,500 should have been declared as income by her. The deficiency assessment was paid and timely claim for refund was filed. The claim having been rejected, this action was brought in behalf of her estate.

It is contended in behalf of the plaintiff that the item in question is excluded from gross income by the provisions of Section 108 of the Internal Revenue Code, the pertinent provisions of which read as follows:

"Section 108, Income from Discharge of Indebtedness:

(a) Special Rule of Exclusion. - No amount shall be included in gross income by reason of the discharge, in whole or in part, within the taxable year, of any indebtedness for which the taxpayer is liable, or subject to which the taxpayer holds property if -

(1) The indebtedness was incurred or assumed -

(A) by a corporation, or

(B) by an individual in connection with property used in his trade or business. . . "

It is argued that the item in question should be excluded from gross income under the provisions of (a), (1), (B), which have just been referred to.

As is frequently the case with tax statutes, the phraseology of this section is somewhat cryptic and obscure, and it must be analyzed with meticulous care in order to determine its meaning. The Court is informed by counsel on both sides that the matter now before the Court is one of novel impression. This Court is of the opinion that Section 108 must be read in connection with Section 61 of the Internal Revenue Code, which enumerates a series of items that must be included in gross income. Item number 12 is "income from discharge of indebtedness". That must necessarily mean that if a person pays an indebtedness at less than its face value, the difference is income to him and should be included in gross income. Section 108, however, excludes such a gain under certain circumstances: one of them is a case in which the taxpayer is a corporation; another that is claimed to be applicable here is, if it is received by an individual in connection with property used in his trade or business.

The type of income to which Section 108 as well as Item 12 of Section 61 refers, is illustrated in Kentucky and Indiana Terminal Railroad Co. v. United States, 330 F. 2d 520. In that case, a corporation that had issued bonds payable in pounds sterling, paid off the bonds in an amount in dollars less than the bonds would have called for initially, by reason of the fact that the corporation was able to acquire pounds sterling at a reduced rate. The difference was income, but was held excludable from gross income by virtue of the provisions of a section that was a predecessor of Section 108.

In this case, as is claimed by the Government, the payment made by the lessee of the property was in the nature of additional rent. Clearly, if it had been paid directly to the lessor, it would have been income to the lessor. The mere fact that the lessor might have used the money so received to discharge the amount due on the property would have been immaterial. The circumstance that in order to avoid circuity of action, the arrangement in this case was that the lessee should pay the amount due on the mortgage directly to the mortgagee, does not change the nature of the transaction.

In view of these considerations, the Court reaches the conclusion that the payment of \$27,500, being additional rent, was income to the lessor and that it is

not excludable from gross income under Section 108, since Section 108 applies only to cases in which an obligation is discharged at less than its face amount and income thereby results in the amount of the difference.

Accordingly judgment will be rendered in favor of the defendant dismissing the complaint on the merits. A transcript of this oral decision will be treated as the findings of fact and conclusion of law. Counsel may submit a proposed judgment.

Alexander Holtzoff
United States District Judge.

December 4, 1968.

[Caption Omitted in Printing]

JUDGMENT

This cause having come on for trial by the Court on December 3 and 4, 1968, and having been submitted upon a stipulation of facts and one item of documentary evidence, and the Court having considered the same, as well as the arguments and briefs of the respective parties, and having ~~fully given~~ ^{delivered} its opinion setting forth its conclusions in the premises and embodying its findings of fact and conclusions of law, it is

ORDERED, ADJUDGED and DECREED that judgment is hereby entered in favor of the defendant dismissing the complaint on the merits.

Dated this 20 day of December, 1968.

Alexander Holtzoff
United States District Judge

Approved as to form:

W. Bernard McDonnell
Attorney for Plaintiff

[Caption Omitted in Printing]

MEMORANDUM OF POINTS AND AUTHORITIES IN SUPPORT
OF MOTION FOR A NEW TRIAL, FOR AMENDMENT
OF FINDINGS OF FACT AND CONCLUSIONS OF LAW

Statement of Material Facts

Under the Will of Philip G. Affleck, Deceased, the estate of the decedent was devised to his wife, Grace B. Affleck, the tax payer in this case, for her life, subject only to maintenance of the real estate, payment of taxes and assessments and interest on existing or future incumbrances of the real estate. She had no right to divert to her own use any of the principal of the estate and, as has been stipulated, no obligation to pay off any incumbrances on the estate property. (Last Will and Testament of Philip G. Affleck, ITEM III).

At her death, the estate was bequeathed to a named trustee (for whom John H. Polkinhorn, plaintiff herein, is the substituted trustee appointed by the court in Civil Action No. 2582-59) for the joint lives of two designated income beneficiaries and their issue, if any, during their minority. After the death of the two named income beneficiaries without issue or at the date all of the surviving issue attained the age of maturity, the entire trust estate was bequeathed to the Duncan Memorial Methodist Episcopal Church and the Grace Episcopal Church, both of Berryville, Virginia in equal parts. (Last Will and Testament of Philip G. Affleck, ITEM IV).

The lease dated September 28, 1960, made by Grace B. Affleck, the life tenant, and John H. Polkinhorn, testamentary trustee under the Will of Philip G. Affleck, as lessors, approved by resolution of the vested and contingent remaindermen, provided, as part of the total rent payable by the lessees, "discharge by the tenant" of the lessor's indebtedness of \$27,500 secured by deed of trust on the leased land. (Lease, page 1). The lessee assumed the lessors' obligations for repayment of principal and the payment of interest on three certain promissory notes secured by deed of trust to the leased premises, the lease reciting that such notes were payable at the office of the American Security and Trust Company, Washington, D. C. (Lease, Subpart I, Paragraph 6, page 3). The discharge of the aforesaid indebtedness was to occur before the existing improvements were razed. (Lease, Subpart I, Paragraph 7, page 4). All other payments of rent were to be made to the rental agent designated by the lessor.

The \$27,500 indebtedness was discharged by the lessee by payment in 1960 of the full amount of three promissory notes to American Security and Trust Company (Stipulation)

Points and Authorities

I

1. The Court's conclusion of law that the \$27,500 paid by the lessees to the bank holding the notes secured by property of the estate was taxable income to the lessor is erroneous and

contrary to the provisions of Section 108(a) of the Internal Revenue Code of 1954.

The Court in its opinion has found and concluded that Section 108(a) of the Internal Revenue Code of 1954 is "cryptic and obscure" and has read it in connection with Section 61(a)(12) in order to determine its meaning. By attempting to modify the language of Section 108(a) by the language of Section 61(a)(2) the Court has erred.

Section 61(a)(12) defines generically discharge of indebtedness as income. It applies to all species of discharge, whether in whole or in part, whether of individuals or of corporations, whether personal or in connection with trade or business, and whether by forgiveness or cancellation by the creditor or by payment by the debtor or a third party.

The Court has selected one such species of discharge of indebtedness--payment of indebtedness at less than face value--and says that the difference is income and includable in gross income, and that Section 61(a)(12) necessarily means this. The same can be said of all of the various species of discharge of indebtedness, including payment in full by a third party, as occurred in this case.

But it cannot be said, as the Court does, that any one species of income resulting from discharge of indebtedness included in Section 61(a)(12), it is therefore meant to be excluded from gross income by Section 108(a).

Section 108(a) selects, out of the various species of income included in Section 61(a)(12), certain income resulting from discharge of indebtedness, in the case of indebtedness of a corporation, or of an individual if incurred or assumed in connection with property used in the individual's trade or business.

Such language is clear and unambiguous. It does not limit itself to payment of indebtedness at less than face value, nor to cases of cancellation or forgiveness by the creditor.

The Court has equated Section 61(a)(12) and Section 108(a) gratuitously and has cited Kentucky and Indiana Terminal Railroad Co. v. United States, 330 F. 2d 520, as supporting such a position and as limiting the application of Section 108(a) to cases of payment of indebtedness at less than face value. In that case, the debt was discharged at face value, in pounds sterling, and the court went out of its way to reject the Government's attempt to limit the privilege of exclusion of income from discharge of indebtedness in any way whatsoever.

II

The Court's failure to make a finding of fact or conclusion of law, or both, as to whether the \$27,500 was income to the life tenant or to the whole estate is logically defective, fails to resolve a principal issue raised by the complaint and the facts of the case, and leaves the case in an incomplete posture for a dispositive ruling by the appellate court.

The 99-year lease, under which the \$27,500 payment was made to the creditor of the estate by the lessee, was a lease made by the life tenant and the trustee of the ensuing estate, and approved by the remaindermen themselves, in whose hands the property would come subject to the lease. All of these, collectively were the "lessor" of whom the Internal Revenue Service singled out one for assessment of income tax due, and among whom the Court has not distinguished the beneficiary of what the Court has ruled to be income.

The obligation on the indebtedness was not the obligation of the taxpayer, life tenant, in her individual capacity, but was the obligation of the estate, secured by deed of trust of the fee title to the real estate, which fee title belonged equitably to the remaindermen of the estate, subject to a preceding life estate and a trust estate for the joint lives of two persons and their minor issue. The Court has failed to find that the effect of the discharge of the indebtedness was to increase the equity of the remaindermen in the estate and did not enlarge the estate of the life tenant or the succeeding trust.

Under the Will creating the life estate, trust and remainders, neither the life tenant nor the trustee had any obligation to discharge indebtedness of the estate out of the income of the estate. The failure of the Court to distinguish the income beneficiary of the \$27,500 payment held to be income, and the dismissal of the action seeking refund of taxes

assessed against the life tenant only, implicitly holds that the life tenant was the beneficiary of income and required her to use such income to discharge indebtedness of the estate.

The lease specified that that portion of the total rental represented by the discharge of indebtedness could not be paid to the life tenant (nor to her successor Trustee), but required the lessees to assume the lessors' obligation on the three first trust notes payable to a bank, and required the lessees to pay the principal amount of the notes to the bank before razing the improvement which constituted a part of the security for the loan. Thus all of the lessors insured that the life tenant could not have the benefit of receipt of the \$27,500 additional rental which the Court has held to be income to the lessor but which the Court, by dismissing the suit for refund, has, in effect, held to be income taxable to only one of the lessors, i.e., the life tenant.

Thus by holding the \$27,500 to be income, but by failing to make a finding of which lessor's income it was, the Court has left unresolved the principal issue in the case, that is, whether, if income, it was income to the estate in which the taxpayer had a life interest only, or income to the trust for two life income beneficiaries, or income to the remaindermen whose equity in the trust principal was increased by the amount of the indebtedness discharged.

III

If the \$27,500 was income, it must at some time be distributable. Clearly, it was not distributable to the life tenant, since the terms of the lease prevented it from reaching her hands, and since the will prevented her from diverting to her benefit any of the principal of the estate. Similarly, it was not distributable by the succeeding Trustee to the two income beneficiaries, since it would not come into his hands as net income during his holding of the estate, which began at the death of the life tenant four years after the indebtedness was discharged. It could be distributed only to the remaindermen when the trust estate ceased.

Under established principles of the law of trusts, the income beneficiary of the estate could not divert to her own use money received by the estate to be applied on an indebtedness of the estate, even if the money was derived from sources ordinarily regarded as income. 90 Corpus Juris Secundum 644, Trusts, Sec. 355; Skinner v. Taft, 103 N. W. 702, 140 Mich. 282.

If income, therefore, it was income permanently set aside for the remaindermen, and the vested remaindermen were two charitable corporations. The income thus permanently set aside for them was deductible from gross income in the year in which it was received for purposes of income tax, under Section 142(c) of the Internal Revenue Code of 1954.

W. Barrett McDonnell
W. Barrett McDonnell
Attorney for Plaintiffs

[Caption Omitted in Printing]

Jan 13, 1969.
Motion denied
Waltzoff
(cn)

FILED

DEC 27 1968

ROBERT M. STEARNS, CLERK

FILED

JAN 13 1969

ROBERT M. STEARNS, Clerk

MOTION FOR NEW TRIAL, FOR AMENDMENT OF FINDINGS
OF FACT AND CONCLUSIONS OF LAW

Come now the plaintiffs herein, by their attorney, and move the court for a new trial and for amendment of the findings of fact and conclusions of law contained in the Court's opinion entered herein the 17th day of December, 1968, and, as grounds therefor, respectfully shows unto the Court:

1. The Court's conclusion of law that the \$27,500 paid by the lessees to the bank holding the notes secured by property of the estate was taxable income to the lessor is erroneous and contrary to the provisions of Section 108 (a) of the Internal Revenue Code of 1954.

a. The Court's finding and conclusion that the language of Section 108(a) is "cryptic and obscure" is erroneous, in that the language is unambiguous in excluding from gross and therefore from taxable income all income resulting from discharge of indebtedness if such indebtedness was incurred or assumed by a corporation or by an individual in connection with property used in his trade or business.

b. The Court's conclusion that the language of Section 61(a)(12) of the Internal Revenue Code of 1954 modifies and qualifies the language of Section 108(a) is erroneous in that Section 108(a) carves out of the genus of income from discharge of indebtedness under Section 61(a)(12) two species of such income and excludes it from taxation.

c. The Court's conclusion that the situation involved in Kentucky and Indiana Terminal Railroad Company v. United States, 330 Federal 2d., 520, supports the Court's highly restrictive interpretation of Section 108(a) (and Section 61(a)(12)) is erroneous and reads into the clear and unambiguous language "discharge of indebtedness" a limitation to payment of indebtedness at less than face value.

2. The Court's conclusion that the \$27,500 was income to the "lessor" fails to distinguish between the respective entities and interests of the life tenant, the succeeding trust, and the remaindermen, and thus fails to resolve a principal issue raised in the pleadings and the evidence, and leaves the case in an imprecise and incomplete posture for dispositive ruling at the appellate level.

a. The Court failed to make a finding or state a conclusion of law as to the ownership of the income among the life tenant, the trustee, and the remaindermen, all three of whom were, collectively, the "lessor", so that it can be determined upon which of them the obligation of the tax, if any, should fall.

b. The Court failed to make a finding of fact that the lease expressly provided for payment of the \$27,500 by the lessee directly to the holder of the notes, an entirely different arrangement from that provided in the lease for rent payments.

c. By concluding that the complaint should be dismissed, the Court has erroneously charged the life tenant with the obligation of payment of tax on the income, when no benefit of such income accrued to her and when, in fact, the lease expressly excluded her from receipt of such income.

d. The Court's conclusion that payment of the indebtedness by the lessee direct to the creditor was the same as payment to the life tenant, is erroneous in that (a) it assumes that such payment benefited the life tenant, and (b) it requires the life tenant to pay taxes on benefits received by another.

e. In failing to make a finding with respect to which of the entities and interests comprising the estate received the benefit of the discharge of indebtedness, the court has erroneously failed to apply the provisions of Section 142(c) of the Internal Revenue Code of 1954 to a situation where income has been permanently set aside for a religious purpose and is deductible from gross income for income tax purposes.

3. And for such other and further reasons as may be presented at the hearing on this motion

4. Plaintiffs request an oral hearing on this motion.

W. Barrett McDonnell

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NA. 8-2880

[Certificate of Service Omitted in Printing]

[Caption Omitted in Printing]

FILED

MAR 6-1969

ROBERT M. STEARNS, Clerk

NOTICE OF APPEAL

Notice is hereby given that J. Henry Polkinhorn, Executor of the Estate of Grace B. Affleck, Deceased, and John H. Polkinhorn, Trustee of the Testamentary Trust under the Will of Philip G. Affleck, Deceased, plaintiffs above named, hereby appeal to the United States Court of Appeals for the District of Columbia Circuit from the final judgment entered in this action on December 20, 1968.

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(Telephone: NA. 8-2880)

Copies to:

Asst Atty Gen
Tax Division
Dept Justice
+
US Attorney

